

**Rural**

# COOPERATIVES

USDA / Rural Development

January/February 2003

## Agricultural Cooperatives in the



Are You  
Ready for  
Tomorrow?



## *Assessing the risks and opportunities ahead*

The cover story of this issue provides a summary of one of the most important USDA co-op reports of recent years: “Agricultural Cooperatives in the 21st Century” (RBS Cooperative Information Report 60.) The article (and report on which it is based) presents an overview of what many of the nation’s leading cooperative thinkers believe to be the critical challenges cooperatives must come to grips with if they are to remain viable in the years ahead.

This report reflects the thoughts of 79 cooperative executives, board members, university professors and staff, farm organization leaders, cooperative council members and cooperative advisors, each of whom devoted a day of their time to participate in one of six focus group meetings held across the nation. Their commitment exemplifies the importance they all attached to this exercise, knowing that the margin of error becomes ever thinner in agriculture. For those who do not have a good overview of the road ahead, the odds are slim for a successful journey.

The result of these six days of

*For those who do not have a good overview of the road ahead, the odds are slim for a successful journey.*

intensive discussions is a compendium of the views and ideas—the collective wisdom—of these leaders on the role of cooperatives at the dawn of the 21st century. We at USDA again express our thanks to these 79 leaders and thinkers, whose cooperation represents the type of support USDA has relied on from the co-op community in the 78 years since Congress first mandated that USDA play a key role in increasing public understanding and use of the cooperative form of business.

Does Congress’ encouragement for collective problem solving through cooperatives still have relevance in the 21st century? The answer, from our focus

group members, was an emphatic “Yes!” In fact, they see such action as even more imperative today, given disparities in market power between vulnerable independent producers and the increasing level of concentrated economic power in the food manufacturing/retailing sector and farm input suppliers.

The focus group participants saw governance, capitalization, member relations and benefit-sharing issues as becoming increasingly complex and difficult. But there are rational solutions. Panelists recommended more analysis of these issues by USDA/RBS Cooperative Services through its research, technical assistance and education programs.

Work of this nature by USDA can only continue with support of, and interaction with, the cooperative community. It is your cooperatives that supply the vital economic data (through our annual survey) and provide other information on strategies and business operations, etc., that are so essential to our efforts.

Improvements in the legal framework for cooperation and the building of effective working relationships among cooperatives to strengthen members’ purchasing and marketing power are possible through close interaction between cooperatives and the public sector program that serves them.

Cooperative and farm community leaders, as well as university faculty, devoted valuable time and effort to observe, comment and recommend. Now it is our collective task to respond.

*Randall Torgerson, Deputy Administrator  
USDA Rural Business-Cooperative Service*

### **USDA co-op program leader Torgerson to retire**

Randall Torgerson, deputy administrator for USDA/RBS Cooperative Services has announced his retirement, effective Jan. 10, 2003, ending his career of 29 years at USDA, including 27 years as the leader of USDA’s cooperative program. Torgerson, a native of Wisconsin, left a position as ag economics professor at the University of Missouri-Columbia in 1974 to become a staff economist to the administrator of USDA’s Agricultural Marketing Service. In 1975, Agriculture Secretary Earl Butz appointed him as administrator of the Agricultural Cooperative Service. Torgerson plans to continue to reside in Fairfax County, Va., and to remain active in promoting cooperatives, his lifelong vocation and passion. ■

# Rural COOPERATIVES

January/February 2003

Volume 70 Number 1

**Rural COOPERATIVES** (1088-8845) is published bimonthly by Rural Business-Cooperative Service, U.S. Department of Agriculture, 1400 Independence Ave. SW, Stop 0705, Washington, DC. 20250-0705. The Secretary of Agriculture has determined that publication of this periodical is necessary in the transaction of public business required by law of the Department. Periodicals postage paid at Washington, DC. and additional mailing offices. Copies may be obtained from the Superintendent of Documents, Government Printing Office, Washington, DC, 20402, at \$21 per year. Postmaster: send address change to: Rural Cooperatives, USDA/RBS, Stop 3255, Wash., DC 20250-3255.

Mention in Rural COOPERATIVES of company and brand names does not signify endorsement over other companies' products and services.

Unless otherwise stated, contents of this publication are not copyrighted and may be reprinted freely. For noncopyrighted articles, mention of source will be appreciated but is not required.

The United States Department of Agriculture (USDA) prohibits discrimination in all its programs and activities on the basis of race, color, national origin, sex, religion, age, disability, political beliefs, sexual orientation, and marital or family status. (Not all prohibited bases apply to all programs). Persons with disabilities who require alternative means for communication of program information (braille, large print, audiotape, etc.) should contact USDA's TARGET Center at (202) 720-2600 (voice and TDD).

To file a complaint of discrimination, write USDA, Director, Office of Civil Rights, Room 326-W, Whitten Building, 14th and Independence Avenue, SW, Washington, D.C. 20250-9410, or call (202) 720-5964 (voice or TDD). USDA is an equal opportunity provider and employer.

**Ann Veneman**, Secretary of Agriculture

**Thomas C. Dorr**, Under Secretary, USDA Rural Development

**John Rosso**, Administrator, Rural Business-Cooperative Service

**Randall Torgerson**, Deputy Administrator, USDA Rural Business-Cooperative Service

**Dan Campbell**, Editor

**Vision Integrated Marketing/KOTA**, Design

Have a cooperative-related question?  
Call (202) 720-6483, or  
Fax (202) 720-4641, Information Director,

This publication was printed with vegetable oil-based ink.

**USDA**  
United States Department of Agriculture

## FEATURES



### *4 Meeting the challenge: co-ops in the 21st century*

By John Dunn, Anthony Crooks, Donald Frederick, Tracey Kennedy, James Wadsworth

### *7 Negotiating the crossroads of a new century*

By Randall E. Torgerson

### *10 Annual Reports:*

*How to read them and what they should tell you about your co-op*

By David Chesnick

### *15 What went wrong at Agway?*

*Cornell professors describe how co-op's chickens came home to roost*

By Elizabeth Doran

### *16 Frogs, snakes & kilowatts*

*East Kentucky Power Co-op finds green in environmental program*

By Steve Thompson

### *20 Large co-ops see growth in '01, reverse declining net margins*

By David Chesnick

### *26 Oneida grocery co-op boosts community; helps keep more money on reservation*

By Patrick Duffey

### *31 Local co-ops' net income and sales climb in 2001*

By Beverly L. Rotan



## DEPARTMENTS

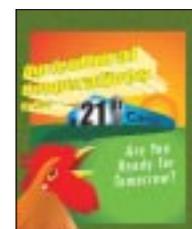
2 COMMENTARY

25 FOCUS ON

34 NEWSLINE

### *On the Cover:*

*On the cover – What will it take for co-ops to compete successfully in the 21st century? The ideas of 79 co-op leaders are summarized, beginning on page 4. USDA graphic by Steve Thompson*



# Meeting the challenge: Co-ops in the 21st century

By John Dunn, Anthony Crooks,  
Donald Frederick, Tracey Kennedy,  
James Wadsworth

*Editor's Note: The authors are all staff members of USDA/RBS Cooperative Services. This article is a summary of recently published RBS Cooperative Information Report 60, "Agricultural Cooperatives in the 21st Century." It is available on-line at the RBS publications Web site: <http://www.rurdev.usda.gov/rbs/pub/newpub.htm>. To receive a free hard copy of the report, send an e-mail request, including your mailing address, to: [dan.campbell@usda.gov](mailto:dan.campbell@usda.gov), or fax requests to (202) 690-4083.*

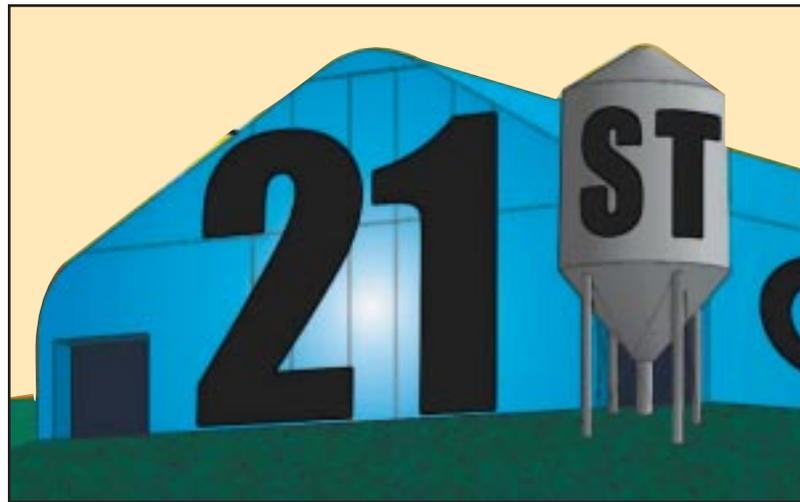
**T**he start of the 21st century is a time of change and challenge for agricultural cooperatives. In late 2001, USDA/RBS Cooperative Services (CS) staff conducted six workshops around the country that examined what cooperatives must do to survive and thrive in the years ahead. Each session consisted of a moderator and 10-15 cooperative managers, directors and advisers. They spent a full day discussing external and internal issues and forces confronting cooperatives and priorities for shaping future cooperatives.

After the last workshop, USDA co-op specialists combined the ideas expressed by the participants with independent research findings by its staff and others into a comprehensive report, "Agricultural Cooperatives in the 21st Century." This article summarizes the observations and recommendations in that report.

## External issues

The world in which cooperatives operate, both on the farm and in the marketplace, is changing at a rapid pace. To remain viable in the 21st century, cooperatives must recognize and adjust to meet the challenges created by the changing marketplace. These include:

**Changing farm demographics.** Fifty years ago, America's farms were predominately operated by traditional family farmers who relied on farming for their income and farmed with the assistance of family members, but little or no hired help. Today, large "commercial" farms that comprise only 8 percent of the farm pop-



ulation generate 68 percent of all farm production.

At the other end of the spectrum, part-time farmers account for 62 percent of the farm population, but generate only 8 percent of farm production. Much of the cooperative system was built to support traditional family farmers. Cooperatives must adapt to a diverse membership that requires different services, products and structures.

**Technological innovation.** Various technology developments are impacting every operation of farmer cooperatives, including:

1. *Transportation.* Large trucks and wide, smooth roads are making obsolete local grain elevators and farm supply stores built to serve farmers who hauled their production to market and their supplies back home in horse-drawn wagons and early pick-up trucks.

2. *Information.* Computers make possible ever-faster collection, analysis and dissemination of information among potential buyers and sellers of agricultural production and food products, shortening the time period in which purchase, inventory and pricing decisions are made. Cooperatives must evaluate their role in a marketplace that values nimbleness, flexibility and information over stationary structures and physical inventory.

3. *Biotechnology.* Biologically based innovations are providing exciting new products, such as ethanol and bio-diesel, bio-polymers and plant-based pharmaceuticals. Historically, improved plant varieties have been developed by land-grant universities and made available to the public at large. Now,

investor-owned firms and universities with large research and development budgets form alliances to patent and profit from their discoveries. Producers and cooperatives are struggling to find a role in this growth area.

**Consolidation and Industrialization.** Consolidation among firms at the processing, wholesale and retail levels of the U.S. food marketing system continues unabated. Dominant retail firms, led by Wal-Mart, are implementing supply-chain management techniques that place increasing burdens on suppliers to provide quality product at the lowest possible price, when and where the buyer wants it. Large food processors, following the lead of poultry marketers, are integrating their operations and dictating how farmers will grow their crops and livestock. As a consequence, even the largest cooperatives are finding it difficult to exert market influence and bargaining strength.

**Globalization.** Communication and transportation developments are leading toward a truly world market for agricultural supplies and products. Farmers and coop-

eratives must learn to do business in an environment where they compete and do business with not only the firms down the street, but also the ones on the other side of the globe.

**Consumerism.** Technological breakthroughs, notably bar coding, are making it easier to identify and track consumer preferences and increasing consumer influence over food marketing. The future of commodity-oriented cooperatives, whose members tend to produce whatever they want and expect their cooperative to sell it for top dollar, may be limited. To be viable in the future, cooperatives must offer products consumers want and that can be sold

for more than the cost of producing and marketing them.

### Internal Issues

As cooperatives strive to meet the challenges of an evolving business climate, they must also deal with issues within their own organization and operation.

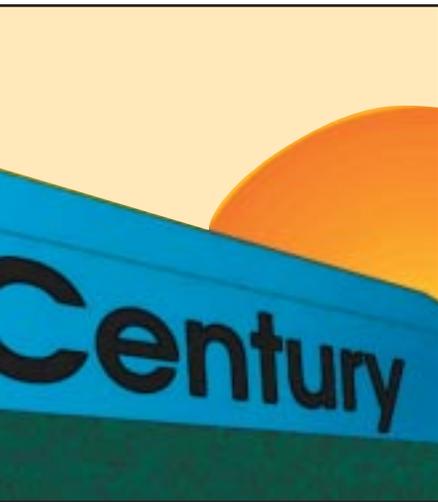
**Acquiring equity.** Cooperative principles limit the opportunity and appeal for non-members to provide equity to cooperatives. Farmers are often either unable or unwilling to adequately capitalize their cooperatives. This saddles cooperatives with weak balance sheets and makes it difficult for them to provide basic services, let alone fund efforts to take advantage of new business opportunities.

**Diverging memberships.** Cooperative memberships reflect the growing disparity among producers. Commercial farmers frequently want different things from their cooperative than do part-time or retired producers. New business strategies may be necessary to satisfy the desires of a heterogeneous membership.

**Board effectiveness.** User control is often implemented by a board of directors composed entirely of producer-members. Many of these directors lack the training and experiences to analyze options for dealing with 21st century issues such as supply chains, technological innovations, complex business arrangements and globalization.

**Federated model.** The federated structure, in which producers form local cooperatives that, in turn, form large regional cooperatives to acquire supplies and market products, is under severe pressure. Many local grain marketing and farm supply cooperatives are not consistently profitable. They expect their regional federated cooperative(s) to be the low-cost source of farm supplies, pay a premium for product delivered for sale and issue a hefty cash patronage refund each year.

Locals are sometimes viewed as unresponsive to the need for change—especially when it comes to closing surplus, unprofitable facilities and to investing in new business opportunities likely to be profitable in the 21st century. Some



## Role of cooperative principles

No definition of a “cooperative” is universally accepted to the exclusion of others. But three basic principles capture the essence of a cooperative enterprise. They are:

- **User-ownership.** Users provide the equity investment in a cooperative and have an ownership claim on its assets.
- **User-control.** Users elect directors and democratically decide other key issues for their cooperative.
- **User-benefits.** Users receive both the services provided and a share of the earnings on the basis of how

much business they conduct with the cooperative.

Other businesses are owned and controlled by investors who focus on maximizing profits. Cooperatives aim to provide quality goods and services to their members at the lowest possible cost, consistent with generating sufficient earnings to keep the business viable. These principles provide some business advantages and justify favorable public policy initiatives. But they also make it difficult for cooperatives to meet certain business challenges, and this is leading some persons to advocate placing less emphasis on them. ■

doubt exists as to whether a system with multiple layers of profit and decision-making centers can take the swift, decisive actions required to succeed in the years ahead.

## Recommendations

Two themes permeate strategies for cooperatives to succeed in the 21st century. First, greater investment is needed in the people who make up cooperatives. Members, directors, managers and advisers must have the skills required to deal with 21st century issues. Otherwise, they will neither completely understand the options available nor have the ability to analyze them and make sound business decisions.

Second, an emphasis must be placed on pragmatism and profitability. Cooperatives are businesses. In the years ahead, they should focus on solving business problems and providing value to their members. If they don't, members will stop patronizing them and they will just fade away.

### 1. Accept and embrace change.

Wishing markets had stopped changing at a certain time, or managing a cooperative as if they had, is a sure prescription for disaster. Industrialization, globalization and technological innovation are here to stay. They are continuously evolving and presenting new and different challenges and opportunities. And as cooperatives move through the 21st century, other developments will have an equal or greater impact. Cooperatives must accept and embrace change.

The recommendations that follow will not be implemented if this one is ignored. Cooperative leaders who refuse to accept change can be expected to take the easy way out when confronted by it: do nothing and hope for the best. Directors, managers and advisers must reject this approach and implement strategic planning programs that systematically look at yesterday, today and tomorrow. We should view "where we have been and where we should be" not as ends in themselves, but rather as foundations for building cooperatives that thrive in the years ahead.

**2. Strengthen cooperative leadership.** Cooperatives need leaders who are prepared to meet the challenges of the 21st century.

Cooperatives must broaden the skills and experiences of their directors. The selection of farmer-directors should be based on ability, not popularity. Directors, once elected, shouldn't automatically serve for life. Longevity can be a criteria for director selection, but it should not be the only criteria. Cooperatives should consider adding outside directors to their boards, especially people with skills in areas where many farmer-directors lack experience, such as food marketing and corporate finance. Grower control is maintained by

giving the members the power to remove outside directors who fail to meet their approval.

Managers must be able to work effectively in a cooperative setting. They may not have the impact on director selection they would in an investor-owned firm (IOF). And as the owners are the users, cooperative managers must accept shareholders walking into their office with often critical comments, while in an IOF, the shareholders may not even know where the headquarters is located. When selecting top management,

prior cooperative experience should be an important criteria.

### 3. Maintain a solid equity base.

Cooperatives must give producers reasons to invest their scarce financial resources. Providing quality goods and services at reasonable prices is part of the answer.

Some farmers are using new and creative financing strategies compatible with cooperative principles. The new-generation model cooperative gives farmer-owners the option to sell their equity to other producers at a market price. This complies with the user-owner, user-control or user-benefit tenets. In other instances, outsiders may purchase dividend-bearing but non-voting preferred stock. While this is a modest departure from strict user-

ownership and user-benefit, it protects the key principle of user-control.

If cooperatives are to be adequately capitalized in the years ahead, either members will need to provide additional funding or cooperatives will have to turn to other sources. The pertinent questions then become, how much capital can farmers provide without jeopardizing their own financial health and how much can cooperatives accept from outsiders without jeopardizing their cooperative character?

**4. Emphasize education.** Cooperative education is an investment and should be viewed as such by both cooperative and public decision makers. While the importance of cooperative education has not diminished over the past few decades, the resources devoted to it have been severely curtailed.

Director training is the No. 1 priority. Without the proper training, the pressure will mount on farmer-directors to abdicate their role as stewards of their members' assets to outsiders with the expertise to run the business but not the appreciation for the importance of the member-user that makes a cooperative special.

Cooperative education is urgently needed for other audiences as well: employees, members, youth, young farmers and the general public. Cooperative leaders have allowed, even facilitated, an across-the-board erosion in cooperative education. In the long run, this can be as



*Tommy Engelke, executive vice president of the Texas Agricultural Cooperatives Council, makes a point during a focus group meeting in Washington, D.C. USDA photo by Dan Campbell*

*continued on page 36*

# Negotiating the crossroads of a new century

**By Randall E. Torgerson,**  
**Deputy Administrator**  
*Rural Business-Cooperative*  
*Service, USDA*

*Editor's Note: The following is excerpted from a speech Torgerson gave at the 57th annual meeting of Tennessee Farmers Cooperative, Nashville, Tenn., in December.*

**T**he general economy and the agricultural sector have been experiencing some of the most trying economic times in our nation's history. The bursting of the technology stock bubble resulted in the longest sustained bear market of recent times. The Sept. 11 terrorist attacks on the Pentagon and World Trade Center and the corporate accounting scandals that have rocked Wall Street have also had a negative impact on the economy and (in the latter case) caused a loss of consumer confidence.

On the farm front, commodity prices in many sectors remain low due to global oversupplies and a more free flow of goods across borders, resulting in a severe cost/price squeeze that is causing many farmers to struggle and to dip into their equity reserves. These have affected farmers' purchasing habits for farm supplies, causing harsh times for input suppliers. In the middle of this year, Congress passed the Farm Security and Rural Investment Act of 2002, pumping substantial direct government payments into the farm economy.

While management of accounts receivable has received increased attention, the high incidence of bad debts has made collections difficult. Interest

rates, a bright spot, have been lowered to help stimulate the economy and remain at the lowest levels in many years, but returns on savings are likewise reduced. Strong real estate prices and recent tax cuts are also credited by some for helping to deflect some of the pain of the bear market.

Our RBS Cooperative Services unit in USDA Rural Development recently reported that net business volume for the nation's 3,229 farmer-owned marketing, farm supply and related service cooperatives topped \$103 billion in 2001. Net income climbed to \$1.36 billion, up over 6 percent from 2000. Farm supply cooperatives saw net income increase by nearly 38 percent, driven by higher margins on petroleum sales.

Farm production supply sales climbed 2.8 percent, with fertilizer and petroleum sales up by over 8 percent, and seed sales up by over 14 percent. Sales of crop protectants, feed and other farm supplies were all down. On the marketing side, livestock, poultry and milk notched the biggest sales gains in 2001, while sales in almost all other agricultural commodities fell. Combined assets of farmer-owned cooperatives reached \$48.5 billion in 2001 and net worth was just over \$20 billion.

With such positive news on the cooperative front generally, why do some express serious concerns about the health of farmer cooperatives?

While cooperatives collectively demonstrated improvement over results in 2000, a number of regionals had low or negative earnings. In particular, the recent Chapter 11 bankruptcy declarations by Farmland Industries, the nation's largest cooperative, and Agway,

a large Northeast regional, have raised eyebrows in the farm community and caused a few skeptics to suggest that cooperatives are an outdated business model. The trade and agricultural press have recently published articles adding to this debate. Headlines I've seen in Northeast and Upper Midwest newspapers include: "Co-ops at a crossroads," "Co-ops challenged" and "Brutal year keeps getting worse for cooperatives."

Obviously, what affects farmers influences the performance of their off-farm businesses: their cooperatives. But all news has not been bad. Poor performance by a few does not indict the cooperative model of doing business, nor does it negate in any way, shape, or form the necessity for farmers to work together for their own economic good. Farmers generally continue to have untapped equity in the rising value of their farms that can be leveraged for productive investments in off-farm, value-added or other endeavors to enhance their farm-related incomes.

The challenge for members, directors and management is to constantly assess the economic environment in which cooperatives are operating and to make the necessary adjustments to keep their cooperative system on the cutting edge to meet members' needs in the most efficient and effective ways possible. This is a tall order given changes occurring in the makeup of production agriculture, farm programs and among the customers and competitors that cooperatives face. But this is the real world in which we live today.

Learning from the experiences of others can help guide your organization. It is a good time to seriously

reflect on some of these basic lessons learned.

### **Maintain a strong balance sheet**

Cooperatives that have found themselves in trouble have often relied too heavily on debt financing. The highly leveraged position has left them exposed during inevitable industry down cycles and unable to withstand prolonged periods of stress, such as we are now experiencing. And too much money that could otherwise be returned to farmers is going into lenders' pockets. Members of cooperatives at all levels—local and regional—need to remind themselves that it is their responsibility to properly capitalize their cooperative businesses.

Don't be afraid to remind members of this responsibility and to ask them for further capital contributions to support their cooperative business. This is especially true when entering new business lines, such as value-added marketing. Members benefitting from such new activity should be encouraged to make capital contributions proportionate to the newly undertaken business activity in which they are participating.

It is difficult for any business to extend itself beyond the carrying capacity of its equity base. When that happens and losses occur, owners stand the risk of credit institutions effectively displacing their governance role and becoming managers of the company store.

### **Reduce system costs**

There is a natural tendency in federated cooperative systems to resist change. A recently completed report by our agency, *Cooperatives in the 21st Century* (see page 4), discusses the heavy pressure on federated cooperatives. The main reason for this is that while farm populations have shrunk, we still have plants and facilities that exceed the needs of the customer base. This translates into maintenance of higher costs within the cooperative system compared to competitors. These costs are seen in redundant assets, under-performing plants and stores, repetitive

handling and transportation of products, and layers of profit centers within the federated system that may be outdated in today's market.

Boards of directors are asked to address these cost issues and to rationalize their local operations by making sure—among other things—that they remain capable of serving the 20 percent of patrons who are doing 80 percent of the business. If they don't, cost structure will remain high as business drops off and members' equity in their cooperative will erode. This situation is happening in too many instances across the country.

### **The "All things to all people" trap**

Each business has its core competencies and knows them. Concentrating on delivering those products and services to members profitably and cost effectively is key to continuing success. Constant assessment of member needs and the actions of competitors is essential to being a survivor in today's business world. Diversifying into business activity unrelated to members' needs or outside the expertise of management can spread the cooperative too thin and run the risk of weakened management controls that lead to losses. It can also lead to membership questions about whom the cooperative is really benefiting, which affects member loyalty. Attempts to emulate the scope of activities of multi-national competitors—or, for example, to "out Cargill, Cargill"—will put members' equity at risk, and the cooperative as well. That is what led to the demise of one of the largest regional cooperatives.

### **Dealing in a mature industry**

Co-ops must realize that all links in the food system are operating on thin margins in a mature industry. Farmers are fewer and larger. Despite growth in farm size and an increase in the number of smaller hobby farms, the total acreage in farming has declined as urban sprawl claims farmland. All market-channel participants faced with this dilemma seek to serve a shrinking market. Often the means of growing market

share is by gobbling up a competitor.

To deal with this situation and stay viable, many cooperatives have extended their base of operations through merger, acquisitions and partnering with other cooperatives. This spreads overhead costs from operations over a broader base while delivering products and services to members more cost effectively. Inefficient or poorly located facilities are closed, sometimes reluctantly, by a board of directors. Much merger activity continues among locally owned cooperatives throughout the country as a strategy to deal with this situation.

Further, a major realignment of feed, fertilizer and petroleum delivery has occurred through joint arrangements among regional cooperatives. Thorough due diligence is required as part of the pre-nuptial process so that unforeseen skeletons in closets are discovered before, not after, combinations are executed. In some cases, cooperatives have taken on partners in totally unrelated lines of business and found these to be not compatible in the long run.

When mergers take place or other businesses are acquired, it is necessary to take steps to fully integrate this expanded business activity into the core activities of the business and operate them on a cooperative basis. Letting these remain outside and "run loosely" often leads to a holding company style of management that can prove ill-adapted to cooperatives. Cooperatives may require more management oversight than other kinds of businesses at all levels to maintain the focus on cooperative objectives. Otherwise, economies of size and scope are not captured from loose confederations that lack effective management controls. Similarly, com-



plexity of the business arrangements can increase to such an extent that, quoting a Dutch source, members have a difficult time “finding themselves in their own organization.”

Growth through acquisitions is common in mature industries and has been practiced by a number of cooperatives, particularly by the largest 100 firms in the food industry. Indeed, there has been a feeding frenzy on small- and medium-sized competitors by the largest 10 food firms. Acquisitions, including those by cooperatives, provide opportunities to expand operations territory, acquire brands and, in some cases, open up a new customer base or new line of business. When negotiating terms of acquisition — as

with mergers—thorough attention to due diligence is required. It is

also necessary to carefully weigh the price and pay-back from such transactions. A number of

troubled regional cooperatives have paid too much for businesses acquired.

Some cooperatives

have also chosen to partner with investor-owned firms through joint ventures to further accessing markets and making prudent use of capital expenditures. Searching

for, and identifying, the right partner involves meeting mutual needs and meeting those needs using win/win strategies. Cooperatives are encouraged to have at least co-equal shares of ownership and control in these ventures. Also, having a predetermined

exit strategy is an important component of entering into joint ventures with outside firms, since many of these arrangements tend to be relatively short lived.

### **Work to keep co-op system viable, strong**

Farmers in the United States have one of the best farm supply-delivery systems found anywhere in the world. It didn't

develop by accident, but rather through farm leadership and management that correctly perceived the need for developing channels of supplies, services and marketing to remote rural communities.

Like all business sectors, farm supply distribution is affected by new technology, such as use of the Internet system as a source of information on prices and other terms of trade. It is also affected by discount chains, such as Home Depot, Lowes and Wal-Mart, that sell supplies in bulk quantities. How this technology and new competition are dealt with requires astute management and boards of directors sensitive to changing buying habits.

Some faltering cooperatives have circumvented their own stores and the local cooperative system by instead relying on dealer networks. While farmers need to assess how much local cooperatives must invest in assets, relying solely on a dealer system of delivery often puts the regional cooperative a step further removed from members and patrons. And dealers are often fickle in their loyalty to the supply sources, opting to move their business for a nickel.

### **Keep up with farming trends**

A key requirement in today's farm supply business is to keep an eye on farming trends. The mid-South region has seen major crop shifts occur as tobacco production has decreased and dairying has diminished. In some states in this region, there are more horses today than there are dairy cows. While the loss of dairies is a blow to many co-ops, the horse industry provides a feed marketing opportunity that could help offset at least some of that loss.

Fertilizer sales continue to be affected by environmental concerns as phosphate levels build up on farms in many states. Crop protectant sales have been revolutionized by the use of Roundup, which changed the whole margin structure in chemical sales. Cotton production grew like gangbusters in the 1990s in the Atlantic states, but has since flattened out. In a number of areas, minor crop production has increasingly provided new business opportunities.

While Internet sales have not yet turned out to be all that was projected, farmers like to price-shop. Providing information can be very valuable to farmers. A very informative Web page will get farmers interested in your cooperative, allowing farmers to visit it afterhours. It also helps locals provide information on services they offer, products and hours of operation.

Global information systems and global positioning system (GIS/GPS) are very important words to farmers. Even if they cannot afford it now, they still want to know that your cooperative is on the forefront of technology. Locals need encouragement to acquire this equipment and, in some instances, to share it when demand is not great enough to support an individual purchase.

Use of crop and livestock production specialists through regional supported programs keeps local employees informed of new products and technologies. Certification of the program and increased use of quality protocols for identity-produced crops shows farmers that there are top-notch employees available to help them understand new technologies. Similarly, employment of marketing specialists to help advise farmers on marketing their output can greatly increase farmer loyalty as well as input sales.

Cooperatives must stay attuned to these trends and strategies to take advantage of opportunities where feasible.

Are cooperatives at a crossroads? In many ways, yes, given the challenging environment and instances of demise. But as shown by the statistics mentioned earlier, cooperatives remain a strong and significant force in today's marketplace. There are both pluses and minuses for co-ops in what I have said here today. Either way, members and directors need to stay fully attuned if they want to properly position their cooperatives for the times ahead. Here are six lessons to keep in mind as we look forward to good years ahead and a continuing strong market presence:

*continued on page 37*

# Annual reports:

*How to read them and what they should tell you about your co-op*

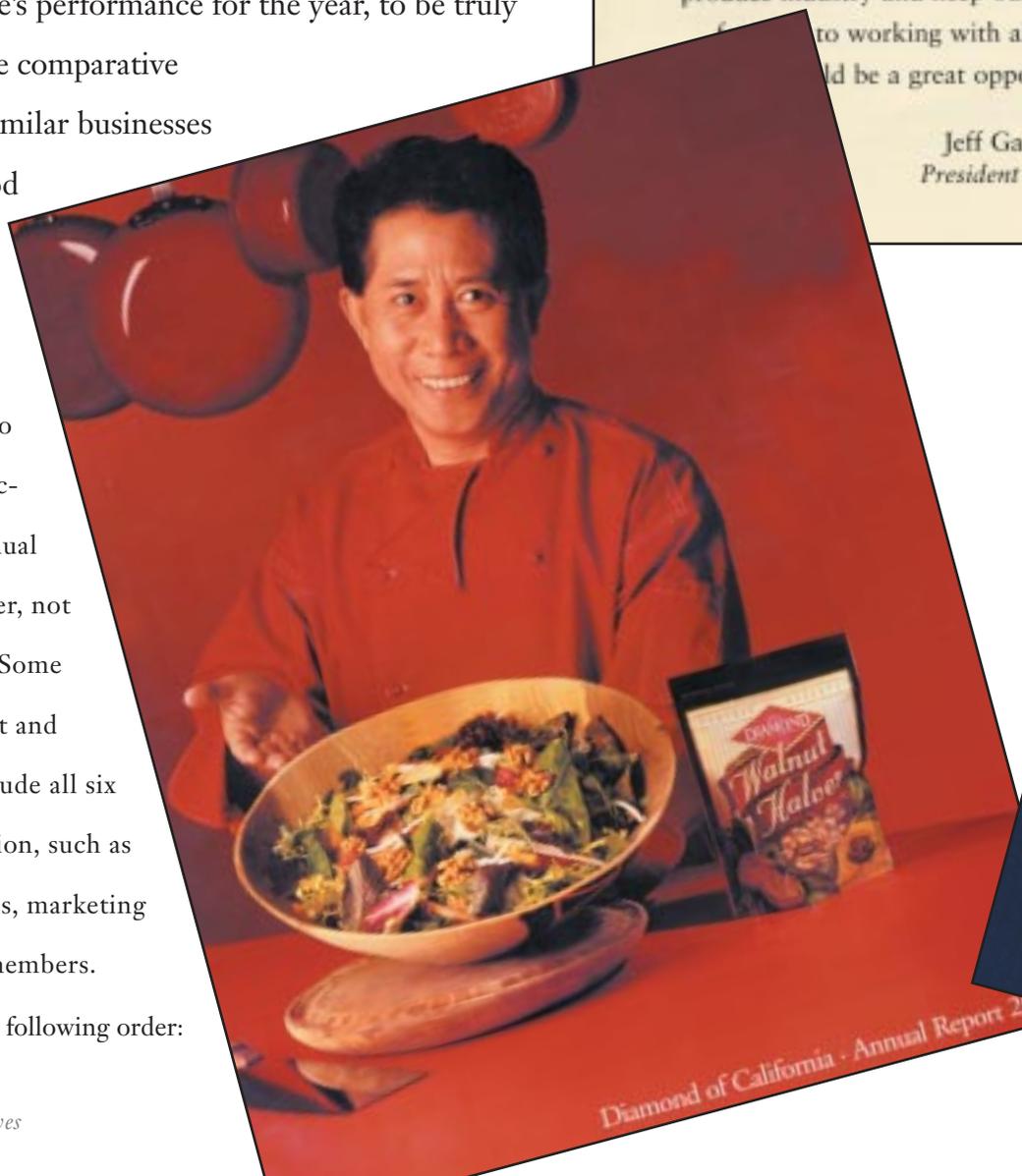
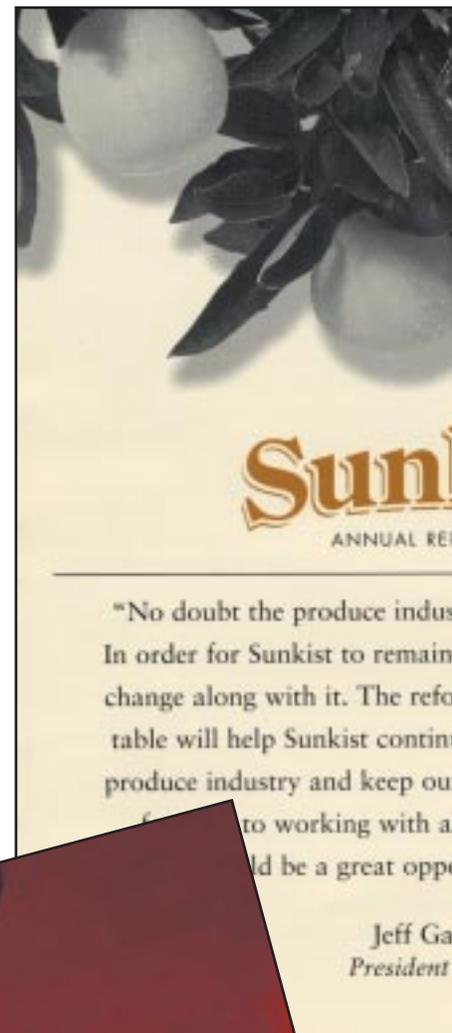
**By David Chesnick**  
USDA/RBS Economist  
david.chesnick@usda.gov

**A**nual reports present information about a cooperative at one point in time. By the time the auditors finish with their work and the report is published, the information is already history. However, they do provide a useful source of information about your cooperative.

While it illustrates the cooperative's performance for the year, to be truly valuable the annual report must have comparative data. The comparison can be with similar businesses or the same cooperative over a period of time. It is also important to keep a calculator, pencil and paper handy for analyzing the numbers.

While there is no single correct way to read an annual report, there are some sections that should be read first. Good annual reports usually contain six parts. However, not all annual reports will contain all items. Some include only a consolidated balance sheet and statement of operations. Others will include all six parts, along with non-financial information, such as overviews of operations and new facilities, marketing efforts and articles focusing on certain members.

The annual report generally flows in the following order:





*Clockwise from top: Sunkist used a statement from its president/CEO on the cover of a recent annual report, while DFA showed a group of members seen through a die-cut window. When folded open, the DFA report shows a drop of milk creating concentric rings and continues the message from the cover with the words "...can affect our entire organization." In the text portion of its report, Diamond of California used well-known chef Martin Yan to demonstrate the joys of cooking with walnuts.*

... is changing very rapidly. competitive, we will have to farm proposals that are on the ue to be a major force in the r growers competitive. I look ll of you in effecting what opportunity for Sunk

...rgiulo & CEO



**DFA**  
DAIRY FARMERS OF AMERICA  
2001 Annual Report

*a single member ...*

1. CEO and/or board chairman's report
2. Management's discussion and analysis of financial results
3. Multi-year summary of selected financial data
4. Auditor's report
5. Financial statements
6. Footnotes

### **Auditor's report**

A good place to start reading the annual report is the auditor's report. This is a statement from the independent auditor letting you know if the figures in the financial statements represent accurately the position of the cooperative and if they conform to the generally accepted accounting principles.

The report can be either non-qualified or qualified. A non-qualified report means the auditors believe the financial reports are free of material misstatements. If the report is qualified, the auditor will usually spell out what its concerns are in relation to the numbers that are reported.

### **CEO/Chairman's report**

Next, examine the CEO/chairman's report. This report is usually a summary letter that will outline the co-op's performance of the past year and provide some indications of the plans for the cooperative's future direction. The letter should be clear, precise and honest about the ups and downs for the past year. It should also briefly describe major plans for the next year.

A good idea is to compare last year's letter with this year's. Compare what the CEO delivered against what was promised during the previous year or two. If the CEO was fairly accurate last year, there is a good chance that he or she is on top of the situation concerning the cooperative's business. If the trend is to consistently over-promise and/or under-perform, then it might indicate that the CEO or president isn't being totally honest with members or doesn't have a complete handle on the cooperative's situation or its operating environment.

### **Management discussion and analysis of financial results**

While the CEO/chairman's report provides a summary of operations, the management's discussion and analysis should support that summary while filling in the details of operations. This section also tends to be written in more cautionary style than the CEO/chairman's report and should be read in conjunction with it. This will usually look at what significant changes occurred during the past year.

This section should focus on each segment of the cooper-

ative's business, including operations and financial position. It may also include an analysis of the market and competition.

### Multi-year summary of selected financial data

It is unusual for a cooperative to find sudden success or failure in one year's time. Even in the often volatile world of agricultural commodities, situations that create a "failure" or "success" scenario usually develop slowly, and the trends can typically be identified by comparing the co-op's performance over several years.

A multi-year summary of selected financial data will show the company's performance over the past few years. If the annual report doesn't have this section, prior annual reports can be used, as will be discussed in the next section.

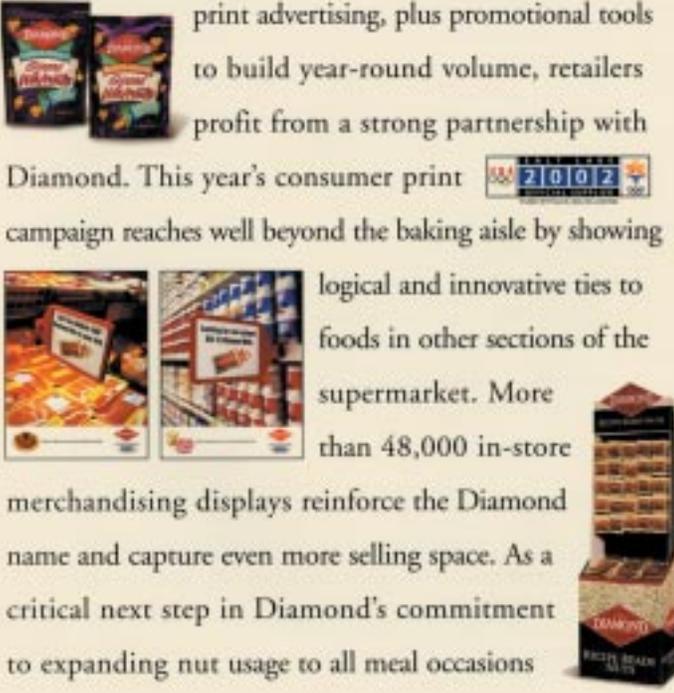
This section usually provides a quick overview of the cooperative's financial trends. Usually it will include 3-5 years' worth of comparisons. This section may include sales, gross margins, net margins, assets, debt and equity. Other information that might be included is per-unit comparisons.

For example, a dairy cooperative could have its financial data compared on a hundredweight basis. This section might also include sources of patronage distribution and allocation. For example, how much income was allocated to members per bushel of grain delivered or gallons of petroleum purchased? Financial ratios might also be found in this section. Checking a company's financial trends over several years provides a meaningful picture of where the company has been and is heading. It also puts into some perspective the CEO's report and management's discussion and analysis as to the future direction of the company.

### Financial statements

By now, you should have a good idea of how the cooperative performed during the past year and where it is heading. The financial statements should support the prior sections and provide the details. If the annual report did not include the CEO's report, management's discussion or multi-year summary, then you will need to get out your pencil,

Diamond's powerful retail presence comes from relentless commitment to brand support. As the only tree nut brand backed by national television and print advertising, plus promotional tools to build year-round volume, retailers profit from a strong partnership with Diamond. This year's consumer print campaign reaches well beyond the baking aisle by showing logical and innovative ties to foods in other sections of the supermarket. More than 48,000 in-store merchandising displays reinforce the Diamond name and capture even more selling space. As a critical next step in Diamond's commitment to expanding nut usage to all meal occasions



Another inside page from the text portion of Diamond of California's 2001 annual report, highlighting some of its retail marketing efforts.

paper and calculator.

The best way to look at the financial statements is to compare them over time. So pull out the annual reports saved from the past few years. Financial analysis is beyond the scope of this article and there are many good books that cover this topic in detail. However, a brief overview of things to look for follows.

- Look at the balance sheet. This shows what the cooperative owns (assets) and who lays claim to those assets (liabilities and equity). The first concern should be liquidity. How has the cooperative's liquidity been moving over time? Variations in a cooperative's liquidity are normal. What should be a concern is a downward trend. If there is a trend, either up or down, look at the individual components of current assets and current liabilities and see what is causing the movement. Declining liquidity could pose trouble in the short run

and cause problems raising operating capital.

- Next look at leverage. Leverage is the use of borrowed funds to capitalize the cooperative. High levels of debt in and of itself do not mean problems. Most fixed assets are purchased with a combination of borrowed funds and equity capital from members. There is a problem if leverage continues to increase while operations stagnate. This trend could indicate that the cooperative is borrowing funds to finance operations.

- Looking at how a cooperative uses its assets provides a look at efficiencies. Turnover ratios illustrate how well a cooperative uses its assets to generate sales or how well they control the assets. When a trend is spotted, it is important to look behind the numbers and see what is causing the trend. For instance, a sharp decline in fixed asset turnover would imply the cooperative sales are not supporting its investment in its fixed assets. Or it may indicate that the cooperative has invested in its fixed assets in anticipation of future growth. The current operations may not fully utilize the expanded assets, which will suppress the turnover ratio.

- Sales, inventories and receivables are three important values to be investigated. Viewed individually they are important, but taken together they tell a good part of the co-op's opera-

tional story. If inventories are increasing at a faster rate than sales, the company could be experiencing unanticipated inventory buildup. This is not a good sign. If receivables are rising faster than sales, the company is not collecting its bills. It may be a sign of deeper problems.

- When focusing on the operating statement, look at sales, gross margins, expenses and net income from operations. What is the trend here? Are sales increasing, decreasing or flat? If sales are falling and there are no clues as to why, then management should be questioned as to why this is happening. Declining sales don't always mean a bad year. Just like higher sales don't necessarily mean a good year. If sales are declining because the cooperative is consolidating operations and focusing on core businesses, the cooperative could be more competitive overall.

- "Common-size" the operating statements over the past few years. That is, divide all values by total sales. Common-sized statements examine what each component of the statement contributes, or takes away, from operations. Be weary of one-time changes in income. See if expenses are consuming a larger portion of sales.

- If the financial statements have a cash-flow statement, this is an excellent area to see how cash is moved around within the cooperative and indicates, in understandable terms, a cooperative's sources and uses of funds. Instead of

digging into every number here, look at the total cash flow from operations, financing and investing. Note how these have been trending over time in each of the three sections. Positive cash flow from operations over time show that operations are strong. Cash flow from investments should tend to be negative. Cash flow from financing should be neutral over time. Of course, this is general. If there are differences, look deeper and *ask questions*.

#### Foot notes

Last, but not least, are the foot notes. The notes that follow the financial statements should be read in conjunction with them. The notes provide a detailed description of what some of the numbers in the financial statements mean. This is where the auditor reports changes, problems, deviations and other anomalies.

These footnotes are often more revealing than the raw data. Watch out for reports of such things as: changes in accounting methods or inventory valuation, new or changed government regulations, debt realignment, litigation results or forecasts and unusual events. Some of these events can have a major impact on the bottom line, either currently or in the future. Most of all, if something is not clear, ask questions until it is clear. You own the cooperative and it is your right to know. ■

## USDA Outlook Conference to focus on critical challenges

A broad array of competitive challenges faced by American farmers in the international and domestic arenas will be examined when the 2003 USDA Agricultural Outlook Forum, "Competing in the 21st Century," is held Feb. 20-21 in the Washington suburb of Arlington, Va. On the international front, experts will examine prospects for increased competition from Central and Eastern Europe, Brazil and Asia, as well as progress in bilateral trade agreements and WTO negotiations. On the domestic front, topics range from the growing complexity and cost of regulations, to market access, to dealing with food safety and changing eating habits.

A year of weather-reduced crops here and abroad underscores the risks farmers face. On the program are a focus session on producers' experience with new crop insurance provisions in effect this year, and a panel of meteorologists discussing weather patterns and the impact on agriculture.

U.S. Agriculture Secretary Ann Veneman will deliver the keynote address, USDA Chief Economist Keith Collins will provide a preview of agricultural prospects for 2003, while FFAS Under Secretary J.B. Penn will look at major U.S. trade and ag policy questions. Dan

Kelly, Growmark chairman, will moderate a panel discussion on competing in the 21st century, and USDA/RBS Deputy Administrator Randall Torgerson will moderate a panel discussion dealing with one of the hottest "growth areas" for cooperatives: livestock producer initiatives. There will be separate panel discussions or lunch speakers addressing market outlook for grains and oilseeds, cotton and fibers, livestock and poultry, milk and dairy, sugar and sweeteners, floriculture/nursery/greenhouse and tobacco.

For the full agenda, visit: <http://www.usda.gov/oce/waob/oc2003/program.htm> .

Registration, including all meals, costs just \$250.

Register online at:

<http://www.usda.gov/oce/waob/agforum.htm> , or by phone: (202) 314-3451.

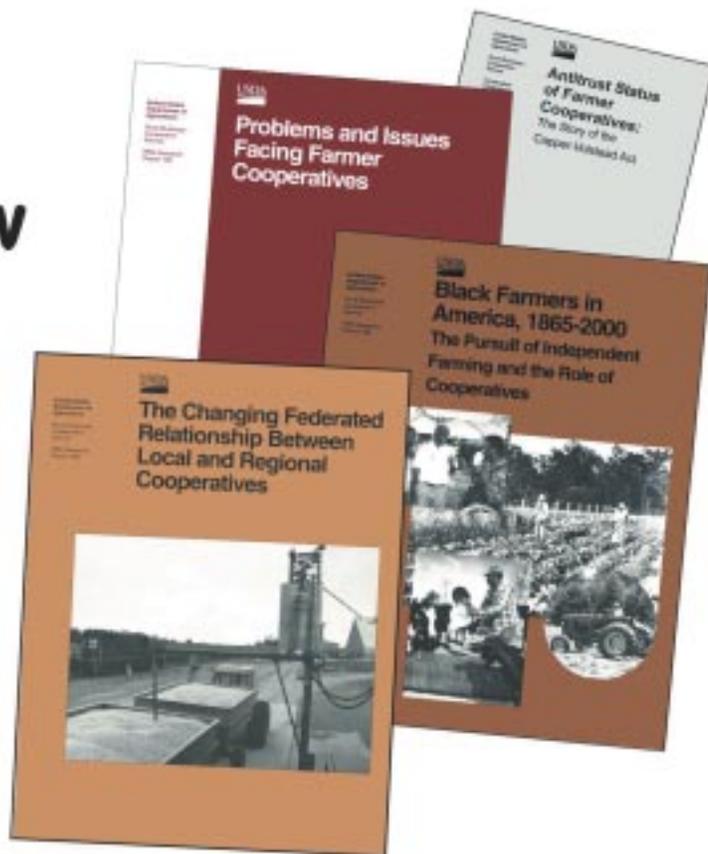
The Forum will be held at the Crystal Gateway Marriott Hotel in Arlington, Va. To receive the discounted room rate of \$144, plus tax, single or double, call the Marriott at (703) 920-3230 and mention the USDA Agricultural Outlook Forum. Discount subject to availability after January 20.

Further questions? Contact, toll free, 877-891-2208 or e-mail [agforum@oce.usda.gov](mailto:agforum@oce.usda.gov). ■

# Stuff

## You Need to Know

If you're a director or manager of a cooperative, or just a co-op member interested in keeping abreast of important issues that affect your interests, these publications offer you important information.



RBS Research Report 192

### **Problems and Issues Facing Agricultural Cooperatives**

Low commodity prices, the sluggish agricultural economy, operational issues, and increasing costs are the major problems facing cooperatives today, according to a survey of 1,147 cooperatives. Find out more in this report. (\$5.00)

RBS Research Report 190

### **The Changing Federated Relationship Between Local and Regional Cooperatives**

Local and regional cooperatives don't always work hand-in-glove; sometimes relationships are strained when local co-ops seek better deals elsewhere. But there are potential solutions, as discussed in this report. (\$5.00)

Cooperative Information Report 59

### **Antitrust Status of Farmer Cooperatives:**

**The Story of the Capper-Volstead Act**  
Without the Capper-Volstead Act, farmers who agreed among themselves on the prices they'd accept for their products would risk being held in violation of antitrust law. But it's not a total antitrust exemption. Knowing the background of the legislation can help co-op officers make the right decisions for their members. (Free for educational purposes)

RBS Research Report 194

### **Black Farmers in America, 1865-2000: The Pursuit of Independent Farming and the Role of Cooperatives**

Learn about the unique experience of American black farmers and the role of co-ops in their struggles for independence and prosperity, from the end of slavery to today. (\$5.00)

Download from our website at [www.rurdev.usda.gov](http://www.rurdev.usda.gov).  
Or fill out the order form below and send or fax to:

USDA/Rural Business-Cooperative Service  
1400 Independence Avenue, SW  
STOP 0705  
Washington, DC 20250-0705

Telephone: (202) 720-8381  
FAX Number (202) 690-4083  
E-mail: [coopinfo@usda.gov](mailto:coopinfo@usda.gov)

Copies of CIR 59: *The Story of the Capper-Volstead Act*  
 Copies of RR 190: *The Changing Federated Relationship* (\$5.00 each)  
 Copies of RR 192: *Problems and Issues* (\$5.00 each)  
 Copies of RR 192: *Black Farmers in America* (\$5.00 each)  
(Make checks payable to USDA)

Name \_\_\_\_\_  
Address \_\_\_\_\_  
City \_\_\_\_\_ State \_\_\_\_\_ Zip \_\_\_\_\_

# What went wrong at Agway?

*Cornell professors describe how co-op's chickens came home to roost*

**By Elizabeth Doran,**  
staff writer  
*Syracuse Post-Standard*

*Editor's note: the following article is reprinted from the Nov. 27, 2002, Syracuse Post-Standard.*

**T**wo Cornell University professors who studied Agway Inc. blame its bankruptcy on a string of financial losses and the company's involvement in too many businesses.

Although they criticize management for its decisions, they also say the cooperative's members bear some responsibility for pressuring management to make bad decisions—such as insisting that local feed plants be kept open even if they were losing money.

And they say there were plenty of warning signs for investors that the company was in trouble. It filed for Chapter 11 bankruptcy protection in October. Bruce L. Anderson and Brian M. Henehan said they analyzed the failure of Agway because of widespread interest from other cooperatives, lenders, extension associates and university researchers.

Anderson is an associate professor and Henehan a senior extension associate in Cornell's Department of Applied Economics and Management. Both have studied the operations of Agway and other cooperatives.

Anderson and Henehan used Agway's annual reports, press releases, filings with the U.S. Securities and Exchange Commission and their own experience in preparing the eight-page

report. Agway had losses in eight out of 19 years starting in 1984, they said in the report, titled "What Went Wrong at Agway." Combined, those losses exceeded profits by \$139.2 million, the report says.

"That says to me that somebody isn't holding someone's feet to the fire," Anderson said. One challenge is figuring how to improve a cooperative's business performance when there are conflicting goals, Anderson said. For example, the cooperative wants to make money, but members don't want to close their neighborhood feed plant.

Which is why, Anderson said, that although management must be held accountable, some of the blame must be shouldered by members who pressured the cooperative to keep local plants open even when it wasn't financially feasible.

"You have to make business decisions," he said.

Although it was Agway's policy not to become involved in dairy processing, the cooperative bought H.P. Hood in 1980, the report says. Agway didn't have any experience running a fluid milk business, and in 1995 sold Hood because of mounting financial losses, the report said.

The report details other factors affecting Agway, including:

- An emphasis in the '70s and '80s on size over profitability;
- A strong link between how much



money members have at risk in the cooperative and the interest they take in the organization. It takes an investment of only \$25 to become an Agway member.

- Reliance on "tax paid retained earnings" as its primary source of equity because equity wasn't coming from members. It can't be sustained without consistent positive earnings.

- Heavy use of debt. From 1998 to 2001, Agway's equity-to-total-asset ratio averaged 12.6 percent, the report said. The professors say when the ratio drops below 15 percent, that usually points to several financial problems.

Stephen Hoefer, speaking for Agway, said problems confronting Agway have been historical challenges, as the report notes. These include being highly leveraged and not having a lot of equity capital, he said. Hoefer also agreed that it's been a challenge for Agway to keep its members involved.

The report highlights many warning signs that should have alerted investors and members to Agway's troubles, the report said. For example, Agway's 2002

*continued on page 38*

# Frogs, snakes & kilowatts

*East Kentucky Power Co-op finds green in environmental program*

**By Steve Thompson,  
writer/editor**  
*USDA Rural Development*

**J**eff Hohman tells you straight out, he loves his job. He's a biologist for East Kentucky Power Cooperative (EKPC), a power-generation cooperative with 16 member electric-distribution co-ops in Kentucky. The co-op pays him to spend many workdays "playing" with frogs and snakes and talking about them to school children.

For the past three years, EKPC has run a wildly popular program with six staff biologists who educate Kentucky school children about local wildlife. They visit two schools in a typical day, presenting lectures and slide shows to up to five classes on each visit.

Meanwhile, most of the co-op's diesel trucks are running on soy-blended "bio-diesel" fuel—which produces fewer harmful toxins and greenhouse gases compared to conventional, straight petroleum-based diesel oil. And the co-op is getting ready to start producing power from recovered landfill gases. It is also exploring wind power and other alternative methods of power generation.

All these initiatives are part of an aggressive effort by the management of EKPC to run an operation that promotes environmental responsibility. "We're showing that power generation, good business practices and environmental responsibility can work hand-in-hand," says co-op president Roy Palk.

## **Nation's lowest power rates**

According to Palk, increasing regulatory pressure and public opinion have pushed environmental issues into the spotlight for the co-op. Coal is readily and cheaply available in the region, and coal-fired boilers generate 97 percent of EKPC's power output. One advantage of coal is low-cost generation. According to the Department of Energy, Kentucky power customers pay the lowest rates in the country.

However, burning coal creates environmental problems, including particulate emissions and nitrogen and sulfur compounds that can contribute to acid rain. Emission problems can be addressed with pollution-reduction technology, including scrubbers, selective catalytic reduction units and new combustion methods. Nevertheless, the co-op felt it necessary to go beyond meeting the letter of current regulations.

"We had no choice but to respond to people's concerns," says Palk. "We couldn't just jump into the bunker."

"A lot of customers on our system are farmers," says Kevin Osbourn, who handles media relations for the co-op. "So using soy oil in our own trucks is a good way to help farmers while we're cutting pollution." The co-op took advantage of a state grant that offsets the 10- to 20-cent per gallon premium on a purchase of 9,000 gallons of bio-diesel.

## **USDA loan focuses attention on wildlife**

While public support is growing for EKPC's green-power initiatives, it is the co-op's environmental education program that has gained the most attention. The program is run on

behalf of EKPC's 16 member distribution cooperatives (see sidebar).

Bill Prather, spokesman for EKPC-member Owen Electric Cooperative, is an enthusiastic proponent of the program. "It's a wonderful experience for the students; it really energizes them," he says. "And it's a great reflection on our co-op." That's because each lecture is given in the name of the local distribution co-op. And Prather notes that the students of today are tomorrow's co-op members.

Hohman, who oversees the lecture program, has a degree in biology, but he originally worked for the co-op as a chemist, analyzing the chemical makeup of different batches of coal used in the co-op's boilers. Then the Rural Utilities Service of USDA Rural Development provided the co-op with a loan



*Jeff Hohman, head of East Kentucky Power Cooperative's Natural Resources and Environmental Communications staff, introduces a hog-nosed snake to an elementary school student. Photo by John Gitner, courtesy East Kentucky Power Cooperative*

for new transmission lines, which added to his workload.

Under the terms of the USDA loan, the co-op was required to report on the impact of the new construction on local wildlife. The task fell to Hohman and several co-workers. He took to walking the transmission lines on Fridays and weekends after his regular work was finished, and collected a few animals as part of this work.

Hohman says the seed for the education program was planted when he was invited to a school “career day,” in which people of various occupations tell the students about their work. He



*EKPC staff members often host nature walks along the co-op's power distribution right-of-ways. Photo by John Gitner, courtesy East Kentucky Power Cooperative*

decided to bring along some live animals to make his presentation more interesting. “It was a huge hit,” he says, and his wildlife lecture was soon in great demand.

Hohman has found a new niche at the co-op. He left the laboratory in 1997 after co-op management decided to create a new Natural Resources and Environmental Communications staff. He now supervises five other biologists. “Jeff’s not the kind of biologist you want to keep in a lab,” says Palk. “He’s articulate and passionate, and a great advocate for environmental responsibility.”

### **Promoting conservation**

The staff does much more than speak in schoolrooms; it’s actively involved in conservation efforts across the state. Co-op biologists spend their

summer months performing biological surveys to determine if endangered species are present. They also harvest seed to encourage the planting of native wild plants.

The staff harvests and packages native wild grass and flower seed and provides it to garden clubs, conservation organizations and individuals for planting in fields and along roadways. The environmental staff also maintains a Web site that offers, among other things, instructions for building houses for bats.

Hohman’s staff also launched a volunteer program called “Frog Loggers,” which recruits people to survey the local frog population (see below).

EKPC has won a number of awards from local environmental groups. But Prather seems less interested in the awards than in the impact they have on the customers of Owen Electric Cooperative, a power-distribution co-op which is a member of EKPC. He points out that a quarterly survey taken by the distribution co-op consistently shows that its members are interested in environmental issues. “It’s a valuable theme to use in communication with our members,” he says.

Prather has other reasons for supporting EKPC’s green initiatives. Knowing that the power-generation co-op is taking concrete action to improve Kentucky’s environment “just makes you feel good,” he says. “We view it as part of our commitment to our community. It’s part of making the area we serve a better place to live.”

### **Toyota request gets ‘eco’ ball rolling**

EKPC’s landfill methane-recovery project is a vivid example of this commitment to environmental stewardship. The project sprang from a request by a major customer of one of its member co-ops.

Toyota Motor Manufacturing North America Inc. headquarters is located in Erlanger, Ky., and is served by Owen

Electric. Owen turned to EKPC when Toyota asked for a renewable source for much of the 130,000 kilowatt-hours of power consumed every month by the laboratory on its Erlanger campus.

That request led quickly to a “green power” option for Owen Electric customers, which was first offered in January 2002 to homes and businesses. Customers could opt to buy 100-kilowatt-hour blocks, each of which carried a \$2.75 surcharge.

Soon other member co-ops expressed interest in the program as well. In June, Inter-County Energy Cooperative joined the green power program; in July, Blue Grass Energy Cooperative joined and, in August, Clark Energy Cooperative climbed aboard. Other member co-ops have also expressed an interest in the program.

Providing the power from a renewable source was simple enough. EKPC began by buying from another producer, then selling the power, in turn, to the distribution cooperatives. But the generation co-op, which prides itself on the low cost of the power it provides its members, then began exploring ways to generate green power on its own, and possibly to save some money doing it.

### **Reliable power source a must for EKPC**

To make construction of a green-power source economically feasible, co-op management quickly decided that the power source had to provide baseload generation—that is, the generation had to be both constant and reliable. That left out wind and other sources more suitable as supplemental power sources because of their intermittent nature. Ralph Tyree, a construction engineer project coordinator working in the resource planning department, was given the task of determining if a practical source of renewable baseload power could feasibly be developed. With the help of a consulting firm, he looked at hydroelectric and other sources before finally determining that landfill gas offered a workable solution.

Landfill gas is growing in popularity

as a source of renewable energy. It's relatively cheap, and sources are readily available—every municipality has to put its trash and garbage somewhere. A landfill-gas generator produces power by burning methane gas that would otherwise escape into the atmosphere, where it is 21 times more destructive as a greenhouse gas than carbon dioxide, the gas produced by its combustion (for more information about power generation from landfill gas, see *Vermont Electric Co-op Looks to Landfill for Methane Recovery*, in the Jan./Feb. 2002 issue of *Rural Cooperatives*, on-line at: [www.rurdev.usda.gov/rbs/pup/openmag.htm](http://www.rurdev.usda.gov/rbs/pup/openmag.htm)).

There were a number of potential sites available close to the co-op's main lines. After scouting numerous locations and negotiating with landfill operators, Tyree and the co-op management settled on three initial sites: Bavarian Landfill in northern Kentucky, near Walton, Green Valley Landfill in Greenup County and Laurel Ridge, near London, Ky.

Each landfill will produce from 2.4 to 3.2 megawatts of clean energy initially, with possible expansion later at Laurel Ridge and Green Valley. The gas will be drawn out through wells drilled into the landfill and burned in large reciprocating engine/generator units—similar to stationary diesel generators—each capable of producing 800 kilowatts.

### Not depending on subsidies

Although federal subsidies are available for the production of power using landfill gas, Tyree says the co-op did not take possible subsidies into consideration when calculating costs. "The subsidy programs have to be funded by Congress every year," he says, "and so we didn't think it was wise to depend on them."

Even so, Tyree says that the overall cost of landfill-gas-generated electricity will be competitive with other baseload options. "If we do get a subsidy," he says, "that'll just be icing on the cake."

The landfill-gas "Enviro-Watts" project—run in partnership with participating distribution co-ops—is expected to start construction as soon as the requisite permits are issued, at a cost of approximately \$4 million for each generation plant. EKPC plans to get all the generators on line this summer.

But already the program is attracting a lot of attention, says co-op spokesman Kevin Osbourn. "We wanted to have



*EKPC President/CEO Roy Palk (seated) and Randy Seymour, founder of the Kentucky Native Seed Cooperative, harvest native grass seeds, which will be used along EKPC right-of-ways. The native grasses create wildlife habitat and are easy to maintain. Photo by Kevin Osbourn, courtesy East Kentucky Power Cooperative*

our ducks in a row before we started publicizing the project; so we only started calling attention to it recently. We've been pleasantly surprised at the response. People are really excited."

Prather, spokesman for Owen Electric, is a bit more cautious. Owen began offering green power subscriptions to all its customers in January 2002. He says the co-op has received a lot of good exposure in the local news media, but that hasn't yet translated into customer interest. Out of 48,000 customer accounts, just 100 have signed up so far.

"We didn't expect a huge response, because most people aren't even aware of green power," he says. "But there's a minority who are quite fervent in their desire to buy it."

Prather believes that consumer education will raise awareness and demand, and that the landfill-gas project will also increase interest. "Right now, when people ask where our green power is coming from, we have to tell

them it's from out of state. Often, they're less interested when they hear that. But when we can tell them it's keeping down pollution in their own area, that'll make a difference. One of the landfills is nearby, next to an interstate highway, so we can point to that."

### Evaluating wind power

Eastern Kentucky's commitment to environmentally sound power generation has given Tyree a new job, as full-time head of the Green Power staff, which is also looking into wind-power and small-scale hydro-electric generation. In February 2002, 15 possible wind-power sites were surveyed in the southeastern part of the state, and two were chosen for further evaluation.

After signing agreements with the landowners, the way has been cleared for the construction of two data-collection towers. They will operate for at least several months, after which the information they gather will be evaluated. A decision will then be made about whether to proceed further.

"We don't really know if wind generators are feasible here in Kentucky," says Tyree. "But those two sites offer the most potential." Tyree's office has looked at three possible low-impact hydro-electric sites, and is considering the use of new-technology "micro-turbines," which each generate about 70 kilowatts.

Alternative power sources can go only so far in addressing environmental concerns, so the co-op is also aggressively pursuing cleaner-burning technologies for its coal-fired generators. One initiative is the planned installation of selective catalytic-reduction technology at the plants. This technology works much like the catalytic converters on cars, reducing nitrogen oxides that older technologies, such as scrubbers, don't catch.

The co-op's newest plant, expected to go on-line with a capacity of 268 megawatts in the spring of 2005, will use a new combustion system called a circulating fluidized bed. The new boiler allows the recycling of particu-

## 2-year waiting list for wildlife lectures

EKPC offers three nature lectures to students from kindergarten to grade 12.

The lectures offered include one about reptiles and amphibians native to Kentucky, which includes a chance for the children to handle live, non-venomous snakes, lizards, salamanders, toads and frogs. Another teaches about the several species of bats inhabiting the area, while a third offers a survey of the wildflowers of the state. The lectures are so popular that they have waiting lists of up to two years.

The program reaches about 50,000 students per year—students who take away with them a greater

appreciation of Kentucky's natural world. "We do a 20-minute slide show, and then hand out the animals, says Hohman. "At the beginning, we'll have a bunch of kids that are squeamish about the animals. But by the time we're finished, just about all of the kids will have handled them. It really makes a difference in the way they look at wildlife."

At the end of the session, every child is given a free Earth Day poster issued yearly by the co-op. The current poster illustrates Kentucky dragonfly and damselfly species. Previous posters have included native frogs, butterflies, salamanders, snakes and orchids. ■



late waste until it is fully incinerated, and will burn fuel at lower temperatures, reducing nitrogen oxides. The boiler also is capable of burning tires (many of which currently wind up in illegal dumps), along with biomass as fuel.

### Frogs: an eco-barometer

When Jeff Hohman lets a wide-eyed sixth grader hold a narrow-mouthed toad in his

cupped hands, or convinces squirming junior high school students not to fear letting a corn snake coil about their arms, he's doing much more than teaching them about the wonders of Kentucky wildlife. He's also driving home the point that creating alternative energy sources is good for humans and 'critters.'

Who knows, he may even find a volunteer today for the Frog Logger program, founded by EKPC's Environmental Education staff. This program is now part of the U.S. Geological Survey's North American Amphibian Monitoring Program—an effort to establish a data base of frog populations for monitoring possible future changes in frog numbers.

Frogs, Hohman explains to the students, seem to be particularly vulnerable to pollution, because their skins absorb substances directly from the air and water. In some areas of the world, frog populations are declining for reasons that are not clear, and some researchers believe that changes in frog populations might signal environmental problems.

The effort is run entirely by volunteers. Participants learn to identify different frog and toad species by their calls, and note the species they hear along a set survey route.

And a world that is safe for frogs, Hohman says, is safer for people too. ■



*EKPC's classroom lectures annually teach more than 50,000 students to appreciate Kentucky wildlife, leaving them with a better understand-*

*ing of the importance of preserving local habitat and air and water quality. Photos by John Gitner, courtesy East Kentucky Power Cooperative*

# Large co-ops see growth in '01, reverse declining net margins

By David Chesnick, Economist  
USDA/RBS Cooperative Services

**C**ooperative board rooms were very busy places in 2001. While mergers and acquisitions dominated the scene in the 1990s, joint ventures and limited liability companies were the focus of activity among the nation's largest co-ops at the start of the new millennium.

Several of the larger cooperatives merged some of their operations into new businesses, which had a negative impact on their sales (which are now counted under the new business entity). Other cooperatives, striving to provide additional high-return marketing options for members' products, formed ventures with non-cooperatives to operate value-added processing facilities. Any net margins generated by these ventures were added to the cooperative's bottom line in the way of non-operating revenue.

Total revenue for the Top 100 co-ops climbed 3.8 percent, to \$74.2 billion in 2001, while net margins increased nearly 10 percent, to more than \$502 million. Still, most cooperatives found 2001 a difficult year, with 2002 not showing much of an improvement. Indeed, two of the nation's largest co-ops (Farmland and Agway) filed to reorganize under Chapter 11 bankruptcy in 2002, and several other major co-ops are facing serious financial stress.

However, most cooperatives should come out of these trying times stronger. In order to compete, cooperatives will need to rely less on debt and more on member equity. A stronger equity posi-

tion provides a cushion when the economy dictates a prolonged downcycle, as we currently are experiencing.

Cooperatives also need to determine their long-range goals and try to focus on their individual strengths. There are many ways a cooperative can get distracted from its mission. This is especially true during hard times, when everyone is looking for ways to bring in extra revenue. Cooperatives should resist the urge to be all things to all members, and should focus on those areas where they have a greater competitive advantage.

## Revenue

Total revenue for the Top 100 cooperatives jumped \$2.7 billion, to \$74.2 billion, in 2001 (table 1). Dairy cooperatives, with an increase of \$2.8 billion in revenue, accounted for most of the increase. Prices earned and volume handled both increased for dairy co-ops in 2001. Poultry & livestock, fruit & vegetable and sugar cooperatives also saw their revenues increase in 2001.

Revenue from farm supply sales for Top 100 co-ops declined 2.1 percent, to \$18.4 billion. But co-ops that sell only farm supplies (excluding diversified supply/grain co-ops) saw revenue increase \$621 million. Higher demand pushed up prices for energy products, which fueled much of the increase in farm supply sales.

Diversified supply/grain cooperatives suffered the largest decline in revenue, with a drop of \$942 million from 2000. Part of this decline can be attributed to a large co-op moving some operations to a joint venture with other coopera-

tives and investor owned-firms (IOFs). In a case such as this, sales (for this survey) are no longer attributed to the co-op, although a share of net margins from the joint venture is allocated back to the co-op. Some of the decline was also caused by lower demand for agronomy products.

Most Top 100 grain cooperatives enjoyed higher revenue in 2001, due mostly to higher prices. Crop volume remained steady. However, a few cooperatives had substantial declines in grain sales, and their losses caused revenue for the overall grain sector to remain relatively flat in 2001.

Gross margins were up for the Top 100 cooperatives. However, not all cooperatives fared well in this area. Farm supply cooperatives ended 2001 with lower gross margins, mostly due to higher cost of raw materials. Some co-ops were able to pass along this price increase to their members, but others could not.

Cotton cooperatives also saw gross margins fall. Whether by choice or design, cotton cooperatives did not pass the full decline in prices along to their members. This resulted in a \$44 million decline in gross margins.

Several of the commodity groups marketing member products cut their cost of goods sold. This implies that grain, rice and poultry & livestock cooperatives were paying their members a smaller percentage of their sales to cover higher operating expenses.

## Operating expenses

Operating expenses for the Top 100 cooperatives were up 2.5 percent,

to \$5.6 billion, in 2001. Farm supply, grain, poultry & livestock, rice and sugar co-ops all posted higher operating expenses, which pushed up operating expenses for all of the largest cooperatives.

In these sectors, all but poultry & livestock cooperatives reported higher labor expenses. All the other sectors reported lower labor expenses, which helped keep their total operating expenses below 2000 levels.

### Net operating margins

Net operating margins were up 6.4 percent for the Top 100 co-ops in 2001. However, not all sectors performed well. Most farm supply cooperatives had lower margins, and a few were hit hard by a combination of lower gross margins and higher expenses. This caused substantial losses from operations in 2001 and resulted in the whole sector posting a net loss from operations. Cotton, sugar and rice cooperatives also ended the year with lower operating margins.

Diversified (supply/grain), fruit & vegetable, grain and poultry & livestock cooperatives had substantial increases in their net operating margins. These increases pulled up the net operating margins by nearly 10 percent for the overall Top 100. Each sector had a unique situation that contributed to improved operations.

Responding to the decline in sales revenue, diversified cooperatives were able to control the cost of goods sold as well as to lower their operating expenses. This resulted in a 24-percent increase in operating margins.

Fruit & vegetable cooperatives were also able to control expenses, and to pass most of their increased sales on to their operating margins. Poultry & livestock cooperatives found themselves in a similar situation, but they were not as successful in controlling expenses. However, higher gross margins were more than enough to offset increased expenses.

Grain cooperatives cut their cost of goods sold enough to compensate for stagnant sales and higher expenses.

**Table 1—Consolidated Statement of Operations:  
Top 100 Cooperatives, 2000-01**

	2001	2000	Difference	Percent Change
	\$ thousand			
<b>Revenues</b>				
Marketing	54,991,765	51,893,235	3,098,530	6.0
Farm Supply	18,418,734	18,818,592	(399,858)	-2.1
Total Sales	73,410,499	70,711,827	2,698,672	3.8
Other Operating Revenues	773,525	796,729	(23,204)	-2.9
Total Operating Revenues	74,184,024	71,508,556	2,675,468	3.7
Cost of Goods Sold	67,613,430	65,132,847	2,480,583	3.8
Gross Margin	6,570,594	6,375,709	194,885	3.1
<b>Expenses</b>				
Operating Expenses	5,613,542	5,476,282	137,260	2.5
Net Operating Margins	957,052	899,427	57,625	6.4
<b>Other Revenues (Expenses)</b>				
Interest Expense	(810,127)	(754,924)	(55,203)	7.3
Interest Revenue	94,232	94,276	(44)	0.0
Other Income	323,153	260,288	62,865	24.2
Other Expenses	(92,227)	(114,055)	21,828	-19.1
Patronage Revenue	43,457	34,855	8,602	24.7
Net Margins from Operations	515,540	419,867	95,673	22.8
Non-Operating Rev. (Exp.)	(13,084)	37,184	(50,268)	-135.2
Net Margins	502,456	457,051	45,405	9.9
<b>Distribution of Net Margins</b>				
Cash Patronage Dividends	241,038	220,146	20,892	9.5
Retain Patronage Dividends	368,529	210,548	157,981	75.0
Nonqualified Non-cash Patronage	16,112	19,021	(2,909)	-15.3
Dividends	39,029	47,279	(8,250)	-17.4
Unallocated Equity	(105,846)	(24,643)	(81,203)	329.5
Income Tax	(56,406)	(15,300)	(41,106)	268.7
Total Distribution	502,456	457,051	45,405	9.9

### Other operating income and expense

Interest income and expense, income and losses from subsidiaries, rent, patronage refunds and other items not directly related to operations are included in other "operating income and expense." Revenues and expenses not directly related to operations resulted in \$442 million in expenses, \$38 million less than in 2000.

Most of this decline in expenses is due to other income from dairy and poultry & livestock cooperatives. Income from subsidiaries for these commodity groups, as well as one-time policy changes, helped push up

other income by \$62 million. Other income not directly related to operations reached \$323 million in 2001. Interest revenue was flat compared to 2000 while patronage refunds were up \$9 million.

For the largest cooperatives, interest expense was by far the biggest expense not directly tied to operations. Nearly all cooperative sectors had higher interest expenses in 2001, which jumped \$55 million to a record high of \$810 million. Diversified cooperatives accounted for 40 percent of the total increase in interest expense. Only grain and sugar cooperatives lowered their interest expense.

## Net margins from operations

Net margins from operations were up \$96 million, to finish 2001 at \$515 million. Leading this increase were poultry & livestock cooperatives, which turned a net loss of \$43 million in 2000 into a net gain of \$45 million in 2001. Dairy, diversified, fruit & livestock and grain cooperatives also increased their net margins from operations.

On the other hand, cotton, farm supply, rice and sugar cooperatives all had lower net operating margins. Farm supply and sugar cooperatives ended the year with larger net losses than in 2000. Farm supply cooperatives ended the year with net operating losses of \$100 million.

Non-operating revenue and expenses include extraordinary gains/losses, gains/losses from discontinued operations or accounting changes. In 2001, this equaled a net expense of \$13 million for the Top 100 co-ops, with diversified cooperatives accounting for the majority of the expense. Farm supply and dairy cooperatives were the only sectors that had non-operating revenue.

The bottom line: the largest cooperatives ended 2001 with net margins of \$502 million, up \$45 million from 2000. The leading sector was dairy. While net margins were up for the largest cooperatives, so too were net losses. Fifteen Top 100 cooperatives suffered net losses in 2001, down from 17 in 2000. However, total losses amounted to \$350 million, up from \$254 million in 2000.

## Distribution of net margins

Cash payments to members were up 9 percent in 2001. For those cooperatives that had net margins to distribute, 28 percent was allocated cash payments. This compares to 31 percent in 2000. Seventy-five percent of net margins were allocated back to members in cash and qualified allocated equity, compared with 70 percent in 2000.

Dairy cooperatives allocated more than their net margins. This was due to a substantial amount of previously unallocated equity being allocated back to members of some co-ops.

On the other hand, fruit & veg-

etable and poultry & livestock cooperatives allocated little of their net margins back to their members in 2001, instead adding most of their net margins to a deferred equity account to be allocated at a later date. Poultry & livestock co-ops used net margins to replenish unallocated equity, which was used in 2000 to absorb net losses.

With more margins being allocated

back to members in 2001, non-qualified patronage refunds and dividends were down. Non-qualified patronage refunds were down 15 percent, to \$16 million. Dividends paid to share holders fell 17 percent, to \$39 million.

The 15 cooperatives that suffered a net loss in 2001 deducted some of that loss from deferred patronage, but most of it was deducted from the unallocated

**Table 2—Combined Balance Sheet: All Cooperatives Top 100 Cooperatives, 2000-01**

	2001	2000	Difference	Percent Change
<b>Assets</b>				
<b>Current Assets</b>				
Cash	880,360	704,462	175,898	25.0
Accounts Receivable	5,778,956	6,106,753	(327,797)	-5.4
Inventory	5,865,377	6,228,431	(363,054)	-5.8
Other Current Assets	<u>1,379,382</u>	<u>1,227,134</u>	<u>152,248</u>	<u>12.4</u>
Total Current Assets	<u>13,904,075</u>	<u>14,266,780</u>	<u>(362,705)</u>	<u>-2.5</u>
Total Investments	4,252,517	4,008,108	244,409	6.1
Net PP&E	8,700,579	8,770,000	(69,421)	-0.8
Other Assets	<u>3,058,603</u>	<u>2,808,338</u>	<u>250,265</u>	<u>8.9</u>
Total Assets	<u>29,915,774</u>	<u>29,853,226</u>	<u>62,548</u>	<u>0.2</u>
<b>Liabilities</b>				
<b>Current Liabilities</b>				
Total Short-term Debt	3,341,825	3,775,334	(433,509)	-11.5
Accounts Payable	3,585,340	3,574,155	11,185	0.3
Member Payables	551,684	487,388	64,296	13.2
Patron and Pool Liabilities	1,434,194	1,470,407	(36,213)	-2.5
Other Current Liabilities	<u>1,755,716</u>	<u>1,984,672</u>	<u>(228,956)</u>	<u>-11.5</u>
Total Current Liabilities	<u>10,668,759</u>	<u>11,291,956</u>	<u>(623,197)</u>	<u>-5.5</u>
Long-term debt	7,083,163	6,490,032	593,131	9
(less current portion)				
Other liabilities and deferred credits	1,137,885	1,054,019	83,866	8.0
Total non-current liabilities	<u>8,221,048</u>	<u>7,544,051</u>	<u>676,997</u>	<u>9.0</u>
Total liabilities	<u>18,889,807</u>	<u>18,836,007</u>	<u>53,800</u>	<u>0.3</u>
<b>Minority interest</b>				
Member equity	899,995	891,504	8,491	1.0
Preferred stock	1,794,562	1,790,651	3,911	0.2
Common stock	733,063	731,369	1,694	0.2
Equity certificates and credits	6,050,674	5,964,779	85,895	1.4
Unallocated capital	<u>1,547,673</u>	<u>1,638,916</u>	<u>(91,243)</u>	<u>-5.6</u>
Total equity	<u>10,125,972</u>	<u>10,125,715</u>	<u>257</u>	<u>0.0</u>
Total liabilities and equity	<u>29,915,774</u>	<u>29,853,226</u>	<u>62,548</u>	<u>0.2</u>

**Table 3—Average selected ratios: Top 100 Cooperatives, 2001**

	Current Ratio	Quick Ratio	Debt To Assets	Long-Term Debt To Equity	Times Interest Earned	Local Assets Turnover	Fixed Assets Turnover	Gross Profit Margin	Net Operating Margin	Return On Total Assets	Return On Members Equity
All coops	1.38	0.75	0.62	0.62	3.79	2.88	15.34	15.19	1.14	3.45	7.02
Cotton	1.29	0.68	0.62	0.36	3.27	2.78	22.31	9.83	0.15	3.53	8.03
Dairy	1.32	0.94	0.60	0.35	12.39	5.80	32.15	8.31	1.45	5.81	15.21
Diversified	1.22	0.84	0.73	1.70	1.35	2.18	9.68	10.57	(0.40)	(0.34)	(3.49)
Fruit/ vegetable	1.57	0.69	0.69	0.98	1.73	2.04	11.58	25.60	1.07	2.10	7.93
Farm supply	1.37	0.63	0.57	0.50	1.78	2.30	11.42	14.76	0.32	2.53	6.11
Grain	1.23	0.58	0.61	0.42	2.41	2.21	8.61	13.33	1.47	4.04	10.31
Poultry/ livestock	2.42	2.00	0.57	1.42	0.37	2.75	40.69	9.94	2.88	2.17	(52.90)
Rice	1.69	0.89	0.48	0.33	7.48	2.29	5.48	32.07	2.09	5.11	11.29
Sugar	1.31	0.68	0.66	1.16	1.19	0.93	1.73	27.96	2.16	1.18	(1.61)

account. Losses also generate a net tax benefit, which was again greater than the amount of taxes paid in 2001.

### Assets

Assets for Top 100 co-ops remained steady, at \$30 billion, in 2001 (table 2). However, the makeup of those assets has changed. Current assets fell by \$363 million, due to declining accounts receivable and inventories. Most of the decline in accounts receivable and inventories occurred in the diversified and farm supply sectors. Cash balances for all of the largest cooperatives were up 25 percent, mainly due to dairy and diversified cooperatives.

Total investment reached \$4.8 billion, up 6 percent from 2000. Most of the \$244 million increase was attributed to non-cooperative investment, which increased \$199 million. Almost all of the increase in non-cooperative investment was concentrated in joint ventures and other partnership arrangements between cooperatives and non-cooperative businesses. However, “other investments” declined, which kept the non-cooperative investment below the \$200 million mark. “Other investments” includes items such as notes receivable, property held for sale, marketable securities, leases

receivable and the like. Dairy and diversified cooperatives had the largest increase in non-cooperative investment, at \$256 million.

Cooperative investment, excluding investment in CoBank, increased 3 percent. Most of this increase was concentrated in the diversified and farm supply cooperatives, which accounted for 87 percent of increased investment in other cooperatives. CoBank investment declined by \$5 million.

Net fixed assets fell 1 percent in 2001. With the exception of dairy and diversified cooperatives, all other sectors had less fixed assets. This is not to say that most cooperatives were not investing in fixed assets. Rather, it indicates sales of fixed assets and depreciation were greater than new purchases.

### Liabilities

As was the case with assets, total liabilities remained relatively unchanged in 2001, yet the makeup of the liabilities changed substantially. Current liabilities fell 6 percent, due to decreasing amounts of short-term debt along with other accrued payables.

Short-term debt was down 11 percent, to \$3.3 billion. Leading the decline were diversified, fruit & vegetable, poultry & livestock and sugar

cooperatives. These sectors used \$903 million less short-term debt in 2001. Cotton, farm supply and grain cooperatives required \$463 million in additional operating loans than in 2000. Most of the increases in these sectors were loans from CoBank.

Accounts payable increased 13 percent, and member-payable and pool liabilities rose 1 percent. This is interesting, given that inventory levels fell 6 percent.

Usually, inventory levels reflect payments for those products. For example, farm supply cooperatives had lower accounts payable with lower inventory levels, as would be expected. On the other hand, cotton and grain cooperatives had higher levels of inventories but lower member payables. This would indicate cooperatives might be using working capital loans to pay members for unsold members' products. In fact, short-term debt was higher for both of these sectors.

Dairy cooperatives had a large, 16-percent, increase in member payables. This \$270 million jump in member and pool liabilities was the main reason these accounts were higher. It appears likely this would be the payment members will receive for the successful year dairy cooperatives had in 2001.

Long-term debt, less amounts cur-

rently due, increased \$593 million. However, most of this increase was concentrated within the diversified co-op sector. Large, diversified cooperatives increased their use of commercial banks, as well as issuing their own notes.

The value of Top 100 agricultural cooperatives' minority interest in joint ventures was up 1 percent, to \$900 million in 2001. Dairy cooperatives were the driving force behind this increase, due to some new joint venture processing facilities. Most of the other sectors ended up with lower minority interest.

### Equity

Member equity for the largest 100 cooperatives ended 2001 with no change in the total amount. However, there was some movement between unallocated and allocated equity.

There were also substantial changes within each sector. Farm supply cooperatives used unallocated equity to absorb some of the net losses during 2001. Conversely, diversified, grain and poultry & livestock cooperatives replenished their unallocated equity accounts while revolving member equity. This shifted their equity structure from allocated funding to unallocated funding. Dairy cooperatives provided the impetus for higher allocated equities among the overall Top 100.

### Performance measurements

Performance measurements are based on the average ratio calculated for the largest cooperatives, and are presented in table 3. Average ratios are used here to negate the effect of changes in a few of the largest cooperatives. In other words, when the 6

largest cooperatives generate 50 percent of total sales for all top 100 cooperatives, any changes by these very large cooperatives would be weighted more heavily.

Liquidity remained fairly stagnant in 2001. The average current liquidity ratio moved from 1.37 to 1.38, while the average quick ratio remained unchanged at 0.75.

Leverage ratios provide a more long-term look at the capital and debt structure of a cooperative. The average long-term debt-to-equity ratio increased from 0.59 to 0.62 in 2001. The average total debt-to-asset ratio was 0.62, up from 0.61 in 2000.

The combined effect of stable liquidity and higher leverage ratios illustrate the change in the term structure of the debt held by these cooperatives. In other words, cooperatives appear to be shifting their debt loads from short-term to long-term. Funds generated from operations were higher in 2001 and were able to fund current operations. Therefore, the need for working capital loans was down.

However, some cooperatives changed their debt structure. Expansion of fixed assets slowed down, yet long-term debt continued expanding. This could indicate that some cooperatives were having problems meeting their current obligations or that favorable interest rates made it advantageous for them to restructure their debt towards long-term financing.

Efficiency ratios look at how well a cooperative uses its assets in generating sales. Local asset turnover remained at 2.9. This means that each dollar worth of local assets generated nearly \$3 of

sales. Activity ratios indicate that cooperatives slowed down on their investment in fixed assets. Several commodity groups were able to expand their market through investments in joint ventures. This was especially evident in the dairy sector.

While not an absolute indicator of fiscal health, profitability ratios provide a view of financial strength for a cooperative. Average gross profit margins inched upwards, from 14.9 in 2000 to 15.2 in 2001. However, net operating margins continued to fall, from 1.3 to 1.1. This would indicate either that cooperatives are not able to efficiently handle higher sales, or that they rely heavily on non-operating revenue to support operations.

Return on total assets continued to trend downward in 2001, falling from 3.6 to 3.4. This ratio focuses on the results of their operation without respect to how the cooperative is financed. This reflects lower efficiencies in the use of the cooperative's assets in generating net margins.

Return on member equity is a ratio that measures the return on member investment after all expenses have been deducted, including taxes and interest. This ratio continues to erode. In 1997, the average return on member equity was 14.3. By 2001, that value fell to 7.0.

The average cooperative in the Top 100 produced higher sales in 2001. However, generating these sales was not cost effective for many cooperatives. One exception was the dairy sector, which was able to turn those higher sales into higher margins for members. Higher total debt levels, along with lower amounts of non-operating revenue, put pressure on the bottom line. ■

## Farm Credit Banks merge in Midwest

An overwhelming majority of voting stockholders have approved the merger between a pair of Midwest farm credit associations. The merger consolidates Farm Credit Services of Northeast Wisconsin into Green Stone Farm Credit Services of Michigan. The new firm becomes the fourth largest cooperative bank in the nationwide Farm Credit System. The \$2.5 billion firm will serve 15,536 customers. ■



# Ursa Farmers Cooperative Ursa, Illinois



**Overview:** Ursa Farmers Cooperative (UFC) was formed in 1920 by farmers in west-central Illinois who were seeking to

gain the advantages of volume grain merchandising. This same concept holds true today for the co-op's 2,200 members, who own facilities at six locations located in west-central Illinois, which annually handle a combined total of more than 20 million bushels of grain and has sales of \$60 million. Services have expanded to include sale of livestock feed and seed for corn, soybeans and wheat. The co-op also sells crop insurance through in-house licensed insurance broker Peggy Duesterhaus. With yearly sales exceeding \$65 million and over 82 years of experience, Ursa Farmers continues to challenge itself to be a leader in the field of agriculture opportunities.

**Philosophy:** Ursa Farmers Cooperative does not believe you can wait to see what the future may bring. *"Our cooperative must be aggressive in recognizing the needs of its member-owners and constantly be vigilant to provide solutions or alternatives to keep its members successful,"* says Board Chairman Victor Kerr.

**One Major Challenge:** UFC merchandises its grain into the export market using two river terminals on the mid-Mississippi River. Nearby competitors include corn and soybean processors which, depending on market variables, are often able to pay more than the "river values" UFC pays. As such, UFC does not strive to be a price leader and therefore must

excel in providing a range of member services to keep the cooperative structure healthy and profitable for all.

Farmer members will constantly strive to derive the greatest value from each bushel. Relationships that are formed as a result of having access to a multitude of services will usually outweigh the small price discrepancies on a day-to-day basis. "Ursa Farmers Cooperative continues to grow because it recognizes its role and value to its members," says General Manager Gerald Jenkins. The cooperative's focus has been to build a close working relationship to help each member meet targeted profit levels.

**Marketing or Service Innovations:** UFC has two grain-marketing subsidiaries. Ursa Brokerage Inc. provides producers access to a full line of brokerage tools for merchandising grain and livestock. The brokerage company is represented by a licensed broker, Marketing Manager Roger Hugenberg, and can offer participants the ability to hedge grain and livestock with every available tool.

The second subsidiary is Ursa Farm Marketing (UFM) Inc., formed in 1998 to help members better cope with challenging mar-

kets, complex government programs and generally stagnant or falling commodity prices. This unit is a comprehensive financial marketing partner to the producer. While producers have always received general marketing advice from the cooperative, UFM offers a much greater degree of management assistance. Producer profitability has been the ultimate measuring device for UFM.

Producers are individually consulted to formulate marketing plans based on specific financial goals. Producers work with co-op staff to determine costs of production, expected sales and any program payments and establish whether needed profits will likely be realized. Producers have access to all forms of hedging tools, including both CBOT (Chicago Board of Trade) options and over-the-counter options, futures and elevator-provided hybrid contracts. The co-op's grain broker assists in every function of the production and selling process. Mar-

*continued on page 38*



Grain elevators tower above the Mississippi River at one of the Ursa Co-op's loading terminals, while co-op members check the current grain prices in a co-op office. Photos by Roger Hugenberg, courtesy Ursa Co-op

# Oneida grocery co-op boosts community; helps keep more money on reservation

By Patrick Duffey,  
USDA Rural Development

**W**e don't need to store grain, so why would we want to form a cooperative?"

That was the reaction of one potential member with a fairly narrow view of cooperatives when Margaret Bau suggested the Oneida American Indian tribe consider forming a grocery co-op. A user-owned store on the reservation, she said, could improve food availability, convenience and affordability for members of the tribe. It would also keep more local dollars turning over on the reservation. However, Bau, cooperative development specialist for USDA Rural Development in Wisconsin, had to undertake a two-year co-op education effort before the concept took root and blossomed.

A smaller, privately owned store in the community had folded earlier after the owner died. But none of the area grocery chains were interested in filling the void on the Oneida reservation.

"Early in the process," Bau recalls, "one of the community volunteers expressed disdain for cooperatives. At a co-op exploratory meeting, I questioned her about the sentiment. She replied, 'My elder neighbor said co-ops—yuck! That's for grain elevators!' I sighed in relief. This was an education gap we could bridge, not some deep-seated cultural issue or an injustice inflicted years ago by a previous cooperative. We can deal with co-op education issues."



*Tower Foods is the first tribal-owned cooperative on American Indian land in Wisconsin, and possibly in the nation. It has a potential market of 20,000 consumers. USDA photos by Patrick Duffey*

## Building co-op customer base

Bau, based at USDA's office in Stevens Point, Wis., and other supporters of the co-op concept did their jobs well. Last July, two years after the initial meetings, she joined other advisors and members of the Oneida tribe in opening the Tower Food Co-op. The name derives from the tall water tower that dominates the adjoining business park.

Tower Food Co-op is a modern, rural grocery store and the first of its kind on a reservation in Wisconsin. The new cooperative has a potential of serving 20,000 community members. Wisconsin has 11 Native American reservations, two of which have tribal-sponsored grocery stores. But neither of those stores is a user-owned cooperative.

The store operates with a staff of 15, but only two are full time. By fall, the cooperative had already gained more than 300 members. Annual membership costs \$20, or \$100 for a lifetime membership.

"The reaction of the community was much more positive toward cooperatives than we initially anticipated," said Bill Ver Voort, who since 1999 has been coordinator for Oneida Community Integrated Food Systems (OCIFS), of which the grocery co-op is a part (see sidebar). "Although it will take a while to build our clientele, those who have shopped here have expressed amazement and take pride in having such a store in their community."

The store has 6,000 square feet of display space with 2,000 square feet of storage space. It stocks a wide array of

canned, packaged and fresh foods. This fall, beef from the tribe's 400- head herd of black angus (all natural, steroid free) was added to the meat case. Working with a meatpacker in a neighboring community, the co-op has begun a brisk retail trade in beef halves, quarters and wrapped cuts.

### Laying the groundwork

Jerry Treleven, acting manager of the Oneida Community Development Department, and later treasurer of the co-op board, contacted USDA Rural Development in Wisconsin about the project, which had been under study by tribal leaders since the mid-1990s. Bau made an initial presentation about the basics of cooperatives to an Oneida steering committee of nine community members and tribal employees in June of 2000. It was their first direct experience with cooperatives.

In succeeding months, Bau expanded her presentations to the committee to examine cooperatives and the roles of directors, employees and members. She also made more general presentations about cooperatives to community groups.

Bau researched other grocery cooperative as possible business models—including those handling mostly natural

or conventional groceries and those serving low-income areas. Wisconsin has 30 food cooperatives, most of which sprang to life in the 1970s and 1980s and specialize in natural foods. Two rural co-op stores which sell conventional foods were eventually selected as a model for the Tower Foods Co-op.

"For the next two years, I was invited back about once a month to talk about structuring the cooperative, discuss legal issues, provide director training and talk about recruiting members," Bau says. "The Oneida tribe has very knowledgeable employees, so my services were more of a consulting nature on specific cooperative issues. More often on cooperative development projects, I am used as a facilitator and organizer. So playing the consultant role was new for me. Bill Ver Voort was really the point person."

Ver Voort was familiar with the Oneida tribe even before going to work for them in 1999. As a young man, he farmed land originally within the reservation boundaries. He went on to secure a degree at the University of Wisconsin-Green Bay and spent five years working with nonprofit organizations, including several years in Thailand teaching English and organizing an English-language program at four

colleges. After his return to the United States, Ver Voort went to work for his former neighbors, coordinating OCIFS programs that help the tribe achieve its goal of self-reliance in food production.

The grocery store steering committee included members with business experience, but most were not familiar with a grocery operation, much less a cooperative. However, Parker Plitz, the Oneida Nation's planner, a member of the store's new board of directors and the first to become a member of Tower Co-op, had earlier organized a food-buying cooperative, which provided useful experience.

Although not initially familiar with the cooperative business model, initial store Manager Carl Lorang had 32 years of experience in the grocery business, most of it gained at stores in Green Bay, and he played a key role in getting the co-op going. He had worked for many years with the Super Valu chain of independent grocers, which was eventually selected as the cooperative's food supplier.

Treleven and Ver Voort spent time learning from the manager of Outpost Natural Foods Cooperative in Milwaukee, which serves a specialized, urban market interested in natural and organically grown foods. "That experience was helpful, but the situation of the Oneida tribe is more rural in nature and the community definitely wanted regular groceries," Bau explains.

A market analysis showed the community could support a grocery store in Oneida. Grants were secured and a location in the tribe's business park was selected. A cooperative board of directors was organized and the Oneida Community Market was incorporated in November 2001 to operate as a co-op. At a subsequent community meeting, products, membership fees, store hours and store design were discussed. Contractors were hired to renovate an existing building.

### USDA, others provide funding

USDA Rural Development provided the Oneida Nation with a



Patricia Cornelius, left, manager of the Oneida Apple Orchard, discusses operations with Margaret Bau, a cooperative development specialist with USDA Rural Development.

## Co-op store part of Oneida Food Systems

The Oneida grocery cooperative is the newest part of the Oneida Community Integrated Food Systems (OCIFS) program, which was initiated in 1944 to address development issues associated with poverty and health programs on the Oneida reservation. The goal of the program is to help the Oneida tribe become self-sufficient in food. Each component of OCIFS addresses different food needs in the community.

OCIFS includes a beef operation, Tsyunhehkwa (joon-henk-qua) Center for integrating traditional Oneida agricultural practices with holistic processes, a community apple orchard/store and a small cannery.

The apple operation is an example of how the tribe devotes effort to acquainting youth with agriculture, stressing the importance of growing healthy food and finding natural ways to eliminate pests. The tribe has 4,000 fruit trees on 40 acres.

In the spring, children from the Oneida elementary school are invited to tour the orchard and learn about agriculture. The orchard also offers fresh fruit and vegetables to all Oneida tribe members at lower prices than offered outside the reservation. Food from the orchard is also furnished to the elderly at the Oneida Senior Center.

The concept behind the Tsyunhehkwa Center program consists of four interrelated components: traditional wellness, commercial and community agriculture, commercial food production and community food preservation. The center is designed to integrate the best of traditional Oneida agricultural practices with holistic processes, based on principles of sustainable development (including economic, ecological and cultural factors).

The center also researches and develops indigenous diet and foods and supplies oils and herbs used for medicinal and traditional ceremonial purposes. The holistic health program teaches people to use herbs, gives massages and sponsors educational workshops on compost making, indoor seed-starts, edible landscaping, vegetable gardening, backyard livestock production, salve making and animal care.

The 83-acre site includes barns, organic gardens, a greenhouse, free-range chicken production, a hoop house (an unheated greenhouse to which indoor-bred plants are transferred for finishing), numerous gardens, and 38 head of organically raised cattle.

The Oneida Cannery helps members preserve food by canning, drying, pickling or cooking traditional foods for special meals or celebrations. Seeds and seedlings are provided for home gardens.

The Oneida food distribution program and food pantry, directed by Nori Damrow, who also serves on the co-op board, provides low-income community members with food packages from USDA, each worth about \$100 per person per month. The food pantry focuses on issues low-income community members face, such as education needs, unemployment and low self-esteem.

The Oneida Pantry opened in 2000 and is run entirely by volunteers. Through networking, Paul's Food Pantry in Green Bay helped the Oneida tribe organize its pantry, and both operations trade surplus foods. Fund-raising efforts—such as luncheon specials, soliciting products from area retailers and an auction—help to sustain the pantry. ■

—By Patrick Duffey

Join us for our 9th Annual  
Tsyunhehkwa  
Husking Bee

Sat., October 5 thru Sat., October 12  
139 Riverdale/Cty. J, Oneida, WI 54155  
9 a.m.-6 p.m. • Phone: 869-2707  
Please dress for the weather!  
Don't forget! October 10 & 11! Educational Days!

through its Rural Business Enterprise Grant (RBE) program (see sidebar). Of that amount, \$250,000 was to renovate the existing building, \$142,000 for equipment, \$23,700 for a small-business incubator project (a revolving loan program), and \$45,000 for the innovative solar system which generates 34,500 watts of electricity

*The Tsyunhehkwa Center promotes events such as husking bees to connect tribe members with their traditional farming practices.*



*Solar panels behind the Tower Foods co-op supply energy to run the store's lights and coolers.*

daily to power the store's lights and coolers.

The Administration for Native Americans provided an additional \$78,000 grant to cover the cooperative's building lease for the first two years and some equipment costs. A grant from the First Nation's Development Institute provided \$50,000 for a service road and funds to assist in providing summer employment at the store for Oneida 4-H members.

The steering committee worked with Frieda (Hugo) Clary from the Oneida Grants Office to develop grant

applications. The Oneida tribal budget for 2001 included a \$250,000 loan to the cooperative. The loan will gradually be repaid from store proceeds, starting in November 2004 as the co-op gains its financial footing. The tribe will then use money to lend to other businesses that locate in the 2,000-square-foot business park adjoining the cooperative store. The business park is already home to a U.S. Post Office facility, an office building and a food pantry charity. One prospective future tenant is a traditional native medicine store.

"We expect the co-op grocery will

attract other small businesses," Ver Voort said.

When Tower Foods Co-op officially opened for business, it was thanks not only to USDA assistance, but to partnerships formed by multiple government agencies, guidance from tribal elders and numerous informational and training meetings. Assistance came flowing in from the University of Wisconsin Center for Cooperatives, North Country Cooperative Development Fund, National Cooperative Business Association, the Cooperative Grocers' Informational Network and the Urban Cooperative Innovative School of Human Ecology at the University of Wisconsin. A video about cooperatives from Wisconsin Public Television also proved to be a useful educational tool.

Pat Pelky, president of the cooperative board, said he hopes the store will be "a very sustainable business—part of the atmosphere around the community for years to come."

### **Bison meat featured; tribe building herd**

One important product featured at the co-op market is bison meat, which has strong cultural and dietary significance for American Indians. Bison was, of course, once a staple for many tribes, and the Oneida Nation is building its own herd. It is one of 50 tribal members of the Inter-Tribal Bison Cooperative (ITBC), which has member-tribes in 17 states.

## **Treaty of Oak Creek moved Oneida tribe to Wisconsin**

In the 1838 Treaty of Oak Creek, the federal government deeded a 65,000-acre reservation to the Oneida Nation when a segment of the tribe was transferred from New York to Wisconsin. Tribal lore has it that Oneida runners were sent ahead to scout prospective relocation sites. These scouts reported back that proposed terrain in Kansas was too sandy, so the tribe opted for Wisconsin as more suited to its agrarian needs.

The tribe's land holdings diminished over the years,

and currently comprise about 12,000 acres spread out within the boundaries of the original reservation. The Oneida lands straddle Outagamie and Brown counties, just west of Green Bay, in northeastern Wisconsin.

In recent years, the tribe has been repurchasing some of the lost acres, including a 30-acre apple orchard. The Oneida farming operations cover 7,000 acres, 3,000 acres of which are tillable, with the rest enrolled in various conservation and wildlife programs. ■

## USDA's RBEG program stimulates business creation on reservations, other rural areas

The Rural Business-Cooperative Service (RBS)—part of USDA Rural Development—provides grants under the Rural Business Enterprise Grants (RBEG) program to public bodies, private nonprofit corporations and federally recognized American Indian tribal groups. The grants are issued to these entities, which in turn lend the money to finance development of small and emerging private businesses. USDA grants do not go directly to a business.

Eligible public bodies include incorporated towns and villages, boroughs, townships, counties, states, authorities, districts, American Indian tribes on federal and state reservations, and other federally recognized Indian tribal groups in rural areas. Small and emerging busi-

nesses assisted must have less than 50 new employees and less than \$1 million in gross annual revenues.

Funds may be used for technical assistance (including marketing studies, feasibility studies, business plans, training, etc.), purchasing or leasing machinery and equipment; creating a revolving loan fund for small and emerging business (providing them partial funding for the purchase of equipment, working capital or real estate), or constructing a building for a business incubator. Grants cannot be used for agricultural production, among other prohibitions.

For more information, visit: <http://www.rurdev.usda.gov/rbs/buspr/rbeg.htm> , or call (202) 720-1400. ■



*The Oneida tribal seal is incorporated into the tribe's apple orchard logo.*

In 1997, the Oneida Nation received an ITBC grant of 13 buffalo from the Wind Cave National Park at Hot Springs, S. D. In 2001, it received another grant of 15 female buffalo from Fort Niobrara Refuge at Lincoln, Neb. This will allow the herd to reproduce in numbers that should make it self-sustaining.

Bison meat, introduced at the store a few months ago, will be given an increasing amount of space in the co-op store as the tribe's herd grows. In addition to serving as a spiritual link to their past for the Oneida tribe, leaner buffalo meat is well-suited to the diet of Native Americans. Diabetes is a common ailment on many reservations (nearly half of the Oneida tribe suffer from it). Louis La

Rosa, secretary of the Inter-Tribal Bison Cooperative, says there is some evidence that bison meat may help in controlling diabetes. The store also stocks a 12-foot section of food items for diabetics.

The cooperative advertises as its budget allows. The tribe's internal e-mail system reaches 2,500 people and carries store advertising every week. In-store weekly special sheets are inserted in each customer's grocery bag and every other week an advertisement appears in the Green Bay Press-Gazette. A special "Wall of Values" at the front of the store promotes products on sale each week.

### **Store integrating into tribal community life**

Efforts are being made to broadly integrate the store into Oneida community life. A farmer's market that offers fresh, locally grown produce is operating near the store. It also offers a place for community members to sell other products.

Acting on a suggestion from Ver Voort, the Falling Leaves 4-H club in

Oneida was organized last fall by Jeanne Baum, 4-H youth development leader for Outagamie County. Six 4-H volunteer leaders have already been trained. Only 10 percent of the county's 4-H members come from an agricultural background. The co-op is providing job training for 4-H members and provides the club and other youth groups—including Boy Scouts, Girl Scouts and Future Farmers of America (FFA)—with space for fund-raising activities. Ver Voort asked officials of the nearby Seymour High School to have its vocational shop program build a booth that will be placed next to the store for fund-raising efforts.

The 4-H club, which does not limit membership to the tribe, undertook a tree-planting conservation project as its first activity. Spring plans call for planting an additional 1,000 trees. The club is generating interest among youth in the tribe's agrarian roots and will focus on Oneida cultural activities.

In these and other ways, the Oneida Nation is setting a pattern that could be used by other American Indian tribes nationwide to harness the power of a food cooperative to sustain their members and strengthen ties to nearby communities. ■

# Local co-ops' net income and sales climb in 2001

**Beverly L. Rotan**  
USDA/RBS Economist

**E**ven with near-record sales by cooperatives in 2001, some cooperatives experienced losses. In today's economic climate, many for-profit businesses, as well as cooperatives, have had to pursue mergers, consolidations, staff reductions and even reorganization under the bankruptcy courts in order to survive.

Factors spurring some of these situations included mismanagement, continued fluctuations in costs, low levels of member participation, depressed farm prices, drought, rising operating expenses, outside competition and other forces. Cooperative management must be ever vigilant and aware of a cooperative's strengths and weaknesses as they relate to sales, cash flow, accounts receivable, inventory mix and/or debt.

Some performance factors are within the control of cooperative management, but other factors are not. One way to become aware of the performance of your cooperative is through financial statements and ratios. Ratios that help assess your cooperative's performance include:

1. *Liquidity ratios*—focus on a company's ability to pay bills when due. If liquidity ratios remain relatively high for a prolonged period, too much capital may be invested in liquid assets (for example, cash, short-term investments, accounts receivable and inventory) and too little is devoted to increasing member equity. These ratios should equal one or more.

**Table 1—Financial analysis ratios for all cooperatives, 2000 and 2001**

Ratio	2000	2001
Current	1.35	1.34
Quick	0.68	0.65
Debt	0.44	0.45
Debt-to-total equity	0.81	0.81
Times-interest-earned	2.81	2.90
Total-asset turnover	1.93	1.97
Fixed-asset turnover	6.61	7.11
Gross profit margin	12.70	12.74
Return-on-total assets before interest & taxes	5.54	5.78
Return-on-total equity	7.91	8.70

2. *Leverage ratios*—reveal a company's use of borrowed funds (rather than members' equity for investments) to expand its business. The goal is to borrow funds at a low interest rate and invest in business activity that produces a high rate of return, exceeding the target rate of return for investment. Debt-to-equity ratio measures the long-term solvency of a company by comparing debt to net worth. A company with a high debt-to-equity ratio could have trouble meeting fixed interest/debt payments if business falters or does not grow as planned. Most lenders would prefer this ratio to be 3 or lower.

3. *Activity ratio turnover*—also called "efficiency ratios," measure activity or changes in certain assets. Poor turnover generally indicates resources are invested in non-income-producing assets. The inventory turnover ratio measures how quickly inventory is sold and replaced each year. An inventory

turnover of 12 means inventory is sold (turned over) once each month. The times-interest-earned ratio measures a company's ability to make interest payments on debt. If the ratio does not exceed the interest rate on current debt, the business may not be making enough to pay interest expenses.

4. *Profitability ratios*—vary from industry to industry and should be compared to a company's ratios for prior years/periods. The return-on-assets measures how well a company is using its assets to generate net profits. The return-on-member equity ratio measures a company's return on members' money.

USDA surveyed 294 cooperatives, which provided information for an upcoming USDA research report ("Analysis of Financial Statements: Local Farm Supply, Marketing Cooperatives, 2001," Research Report 197). For the most part, ratios for the surveyed cooperatives remained rela-

**Table 3—Average farm supplies sold and products marketed; change from 2000 and 2001**

	2000	2001	Change: 2000 to 2001
	— Dollars —		Percent
<b>Farm supplies sold:</b>			
Feed	1,376,265	1,402,410	1.90
Seed	229,504	282,319	23.01
Fertilizer	1,486,326	1,755,377	18.10
Crop protectants	1,268,150	1,259,834	-0.66
Petroleum products	2,891,718	3,408,060	17.86
Other	<u>1,149,898</u>	<u>1,164,804</u>	<u>1.30</u>
<b>Total</b>	<b>8,401,855</b>	<b>9,272,804</b>	<b>10.37</b>
<b>Products marketed:</b>			
Grains and oilseeds	5,320,822	5,460,369	2.62
Other	<u>72,487</u>	<u>73,609</u>	<u>1.55</u>
<b>Total</b>	<b>5,393,309</b>	<b>5,533,978</b>	<b>2.61</b>
<b>Total sales</b>	<b>\$13,795,164</b>	<b>\$14,766,182</b>	<b>7.33</b>

tively unchanged from 2000 to 2001 (table 1). Local co-op savings were up 11 percent and patronage from regional cooperatives increased 13 percent in 2001.

About 15 percent of the cooperatives in the data base had losses in 2001. Through patronage refunds, regionals were an important source of revenues and allowed 26 (out of 44) cooperatives that had local losses to instead show net income for the year. Net income averaged almost \$259,000 in 2001, up from \$231,000

in 2000, a 12-percent increase.

The co-ops in the data base were grouped into four categories: small, medium, large and super (table 2). Sales by local cooperatives of major farm supplies (feed, seed, fertilizer, chemicals, petroleum and farm supplies) averaged \$9.3 million in 2001, a 10-percent increase from \$8.4 million in 2000.

Both fertilizer and petroleum sales increased about 18 percent between the 2 years (table 3). The increases were due to the rise in propane prices.

Propane is used to heat farm homes and as a component in anhydrous ammonia fertilizers.

Seed sale averages also climbed sharply, up 23 percent, to \$282,000 per local co-op in 2001. In fact, every category (with the exception of crop protectants) of farm supply sales increased from 2000 to 2001. In the overall scheme of things, not all farm supplies experienced increases in sales—chemicals, machinery, building materials, containers and food sales decreased.

The total sales (from commodity marketing and farm supplies) average rose to more than \$14.8 million in 2001. Marketing farm commodity sales (crops and livestock) showed a small increase in 2001. Grain sales only increased about 3 percent. Even with high market prices and production in 2001, on average, these sales amounted to \$5 million. Service income increased a little over 1 percent.

Both current assets and total assets were up slightly, 7 and 5 percent, respectively, for the 294 co-ops surveyed. Investments increased in property, plant and equipment, inventories (grain/oilseed and farm supplies) and accounts receivable.

**Table 2—Size and type definitions used for respondent cooperatives**

Cooperative size	Definition	Number
Small	up to \$5 million in total sales	92
Medium	over \$5 million to \$10 million	71
Large	over \$10 million to \$20 million	59
Super	over \$20 million	72
<b>Cooperative type</b>		
Farm supply	total net sales from farm supplies	152
Mixed farm supply	from 50 to 99 percent	67
Mixed marketing	from 25 to 49 percent	57
Marketing	less than 25 percent	18

Current liabilities for local co-ops jumped nearly 8 percent during the two-year study period, with patrons' credit balances, taxes payable and accounts payable showing double-digit increases. Revolving equity redeemed had the largest decrease (-14.5 percent) in this category, reflecting multiple causes, including: losses allocated from previous years, some cooperatives didn't need more capital, mergers, capital stock buy-back, etc.

Growth was also experienced in accrued expenses, as well as in current and long-term debt. Cash patronage refunds and seasonal debt decreased.

Cost of goods sold and revenue almost offset each other in 2000, with cost of goods sold rising 7 percent. Cost of goods sold averaged almost 87 percent of net sales. Total expenses climbed about 7 percent in 2001. Utility costs increased the most. These factors may be the reasons some cooperatives had net income losses for the year.

Co-ops in the study had an average of 39 employees (part- and full-time), who earned an average salary of \$24,863. Total employee expenses were up about 6 percent in 2001. Directors' fees and expenses were a small part of total costs. However,

director compensation is an important factor that helps many cooperatives convince producers to divert time each month to helping guide their cooperative. Co-op boards averaged seven members, who were paid an average of \$886 per year.

Local agricultural cooperatives continued to play a vital role in supplying goods and services to their farmer-members and marketing their crops. Local co-ops are also important to rural communities, where they are often one of the largest employers and generate considerable tax revenues for their communities. ■

## Turkey growers grateful for Nebraska, Michigan co-ops

Turkey growers in Nebraska and Michigan were grateful for cooperative markets this past fall. Four years ago, Michigan growers lost their contract when Bill Marr Foods, part of Sara Lee Corp., moved its boning and slaughtering operations to Iowa. That left local farmers with no processing plants in the state. To compensate, they formed Michigan Turkey Producers Cooperative and opened a processing plant at Wyoming, Mich., in 2001. "Today, the plant is a dream come true. It employs nearly 400 workers and processes more than 4 million turkeys a year. The cooperative now has 16 farmers raising turkeys on 43 farms," said CEO Dan Lennon. "Co-op members account for 90 percent of the 4.5 million turkeys raised in Michigan each year. At the moment, the cooperative sells its meat raw, but anticipates cooking meat directly in a couple years," he said.

Meanwhile, west of the Mississippi, the experience of co-op turkey growers in Nebraska has a longer history, but the same gratitude for a cooperative market still exists. The state's turkey industry is a year-round business worth \$35 million annually to the state's economy. While Deb Van Matre has only managed Nebraska Turkey Growers for the past two years, she's been associated with the cooperative and its 20 members for the past 19 years.

The cooperative will mark its 65th anniversary in February. Each member is an independent grower, supplying their own feed, birds and facilities. Each year, they sign a marketing agreement with the cooperative to supply turkeys to the plant at Gibbon. Members elect the seven-person board.

For marketing services, the Nebraska cooperative turns to Norbest cooperative of Midvale, Utah. The majority of the birds are packaged under the Norbest Nebraska-grown label. The Nebraska members receive baby turkeys from a hatchery, raise them from 12 to 14 weeks and produce as many as seven cycles of bird a year. The plant processes about 4 million turkeys a year, or about 50 million pounds. That compares to just 12 million pounds when the cooperative started. Van Matre expects to hit peak production for the 2003 season. The plant employs 225 people and has an annual payroll of about \$4 million.

Van Matre is optimistic about the cooperative's future and expects turkey consumption to continue increasing. "We are looking at future expansion at the plant and considering adding new products. We are in some planning stages now for that over the next three years," she said. ■



*A new, co-op turkey packing plant in Michigan is processing 4 million birds per year. USDA Agricultural Research Service Photo*



## West Central Soy receives value-added ag award

West Central Soy, a subsidiary of West Central Cooperative of Ralston, Iowa, is the recipient of the 2002 "Value-Added Agriculture" Iowa Venture award. The award recognizes significant contributions and leadership in promoting and developing Iowa agriculture.

West Central Soy and its cooperative members have built the largest, state-of-the-art soy diesel facility in the country. A fuel of the future, biodiesel is a clean-burning fuel that meets the toughest pollution standards. West Central will produce 12 million gallons of biodiesel from 12.5 million bushels of soybeans annually at its Ralston facility in Carroll County.

"This is the sixth year we have recognized Iowa ag enterprises for providing jobs, investment and leadership to local economies," says Rand M. Fisher, president of the Iowa Area Development Group (IADG), who presented the award Dec. 4 at the Iowa Farm Bureau annual meeting in Des Moines. "The economic impact of biobased fuels in Iowa is huge. Together, soybean and corn farmers are helping reduce dependency on foreign sources of oil while enhancing air and water quality. The investment by this farmer-owned cooperative will strengthen our state, its communities and the families of Iowa."

IADG, the business development arm for Iowa's rural electric cooperatives, is in a partnership with the Iowa Farm Bureau Federation to advance value-added agriculture to expand economic opportunity and increase farm income. Previous award winners include the Iowa Farm Bureau Federa-

tion, Southwest Iowa Egg, Wells Dairy, West Liberty Foods, Tall Corn Ethanol, Midwest Grain Processors, Quad County Corn Processors and Siouxland Energy & Livestock.

## Upstate Dairy Co-op targets teen market

In response to a national study indicating interest by teenagers in single-serve flavored milk from vending machines, Upstate Farms Cooperative at LeRoy, N.Y., has been pursuing this market at more than 45 schools and universities across the state. Milk sales from vending machines have increased 300 percent. "Intense" chocolate and vanilla are the most popular flavors. Two years ago, the cooperative used 15 machines to conduct test studies in small schools.

"It's proving to be a popular alternative to carbonated beverages," said

Mark Serling, marketing director for Upstate Farms. "The idea for milk vending came after we switched to using plastic bottles. The next step is to bring more product offerings into the schools and other flavors."

## Growmark purchases Agway's agronomy, seed businesses

Agricultural supplier GROWMARK Inc., of Bloomington, Ill., has sealed the purchase of the agronomy and seed business units of Agway Inc., Syracuse, N.Y. The deal includes the assets of Seedway Inc. production facilities, wholesale and retail agronomy facilities plus Agway's equity interest in CF Industries and Allied Seed LLC.

Bill Davisson, GROWMARK CEO, has named Ed Rodenburg, vice president of eastern retail operations, to head the cooperative's new Northeast operations. He had been the cooperative's Ontario region manager in 1994 and later managed the agribusiness of Agri-core in Calgary, Alberta, Canada before rejoining GROWMARK in October.

"As we bring the red and black 'FS' brand to farmers in the eastern United States, I'm confident they will be beneficiaries of the professional people, product and services that create solutions to farmers' unique challenges," Davisson said. "Our vision is to improve long-term farm profitability through innovation and commitment to excellence."

GROWMARK provides agricultural-related products and services to local cooperatives in Illinois, Iowa, Wisconsin and the Canadian province of Ontario. GROWMARK's predecessor, FS Services, was one of the founding



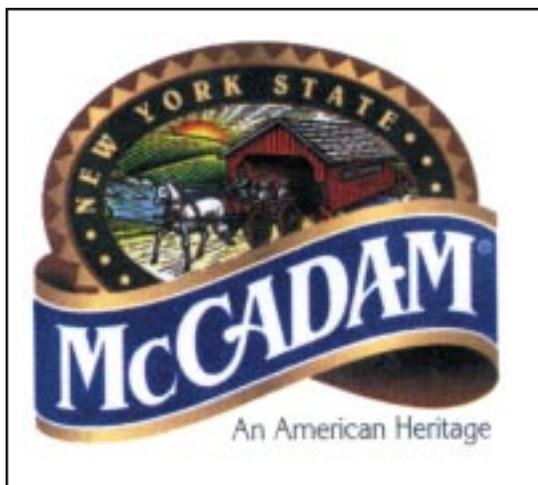
Upstate Dairy Cooperative is having good results using vending machines to sell flavored milk to teenagers. Photo courtesy Upstate Dairy Co-op

cooperatives of CF Industries. Davisson is currently board chairman of the interregional fertilizer manufacturing and distribution cooperative.

Meanwhile, due diligence is expected to be completed by Jan. 1, 2003, in the alignment between GROWMARK's consumer division and Country Depot franchise dealerships and TruServ Canada's chain of cooperative hardware stores. The original letter of intent to align was signed Sept. 11. Details of the combination are pending. GROWMARK has had a presence in Canada since it purchased United Cooperatives of Ontario in 1994.

### Agri-Mark to buy McCadam Cheese

Expansion of its cheese business and merger of a local farm supply cooperative are on the business agenda of Agri-Mark, a dairy marketing cooperative based at Methuen, Mass. Both transac-



tions should be completed by the end of January 2003. Agri-Mark plans to purchase McCadam Cheese at Chateaugay, N.Y., from Valio Limited of Finland, which includes cheese manufacturing assets in which McCadam produces award-winning New York Cheddar cheese, Muenster, Colby and other cheeses, including European varieties.

The deal is contingent upon a merger between Agri-Mark and the 150-member Chateaugay Cooperative, which co-owns the cheese plant with Valio. The farm supply cooperative's board of directors has already endorsed the pact with Agri-Mark, which has

1,400 members in six New England states and New York. Sales reached \$625 million in fiscal 2001. The cooperative markets much of its milk nationwide through its Cabot brand of Vermont Cheddar cheese, butter and other dairy products. The balance of its milk is marketed to dairy processors in the eastern United States. The cooperative owns three processing plants.

The cut-and-wrap portion of McCadam operations at Heuvelton, N.Y., located 150 miles north of Syracuse, will be transferred to Agri-Mark's Cabot facilities in Vermont. McCadam had been shipping cheese from Chateaugay to Heuvelton for storage, curing, packaging and distribution. Brian Lee, McCadam president and manager, lamented the loss of up to 110 of the 130 jobs at the plant. But in the broader view, he said, "the sale by a foreign owner 7,000 miles away to a cooperative of American dairy farmers is a

good thing. McCadam cheese will be available to a wider market." The warehouse and direct-to-store delivery operations will be retained at Heuvelton.

The cheese company was founded there in 1876 by William McCadam. The firm became a wholly owned subsidiary of Dean Foods which purchased it 1972, but then sold it to Valio in 1991.

Paul Johnson, Agri-Mark president, said McCadam's \$60 million in annual sales would complement the Cabot brand of dairy products.

"Nothing is stronger in the marketplace than farmers working together," observed Chairman Carl Peterson. He said the combination would help "propel the McCadam business to new levels of market growth and profitability for dairy farmers." The Chateaugay farm supply store next to the cheese plant will continue to be operated and serve local farmers.

### Farmland gets extension; 2002 losses at \$346 million

Farmland Industries has been given an additional four months, until March 27, to complete and file its reorganiza-

tion plan needed to emerge from Chapter 11 bankruptcy. As of this writing in early December, the co-op was still working to extend agreements with its bankers.

The co-op reported \$346 million in losses for fiscal year 2002. The loss was before taxes, and includes one-time restructuring and reorganization expenses and losses from discontinued operations.

Despite overall red ink, Farmland's refrigerated foods business sales climbed 72 percent, to \$59.7 million, during 2002. Sales were up 3 percent for further-processed meat, an area on which Farmland hopes to pin its future. "Our focus on further-processed meats, including our leadership position on CaseReady pork and beef, strengthened margins considerably," reported CEO Robert Terry. Still pending is the sale or repositioning of Farmland's fertilizer and petroleum assets to erase some of that red ink.

Farmland's sales for fiscal 2000 were \$6.6 billion, down from \$9.2 billion in 2001. The decline was partly due to the formation in 2001 of ADM-Farmland, a grain marketing company wholly owned by Archer Daniels Midland (ADM) but supplied by the Farmland cooperative system. Farmland's grain sales in 2001 reached \$1.7 billion. Terry said Farmland's reorganization plan represented commitments to progress rapidly and thoroughly by working closely with committees representing unsecured creditors and bond holders.

### American Crystal Co-op pays \$34 million for sugar plants

Three sugar processing plants in Torrington, Wyo., Sidney, Mont. and Hereford, Texas, have been purchased by American Crystal Sugar Co. of Moorehead, Minn., for \$34 million from Imperial Sugar Co. The Torrington plant will be leased to Western Sugar Cooperative of Denver. American Crystal will operate the Sidney plant, while the Hereford factory, idled since 1998, will not be immediately reopened. Jim Horvath, American Crystal president, said the additional

acreage and processing capacity at Sidney “will add value to our cooperative’s customers, shareholders and the Sidney community alike.” About 11,800 acres are being harvested for the Torrington plant this year vs. 30,000 acres 2 years ago. American Crystal has two plants in North Dakota and three in Minnesota.

### Graves joins USDA advisors

David Graves, president of the National Council of Farmer Cooperatives, Washington, D.C., is among 11 new members of the U. S. Department of Agriculture’s National Agricultural Research, Extension, Education and Economics advisory committee. He was appointed by Agricultural Secretary Ann Veneman to advise on USDA research,

education and extension policies and priorities. The 30-member board was reauthorized in the 2002 farm bill.

### Improving denim market sparks PCCA rebound

Despite early losses as it exited the yarn-dyed business, Plains Cotton Cooperative Association (PCCA) at Lubbock, Texas, rebounded from a sub-par year in 2001, thanks in part to an improved denim market, President Van May told shareholders at the 49th annual meeting in September. Total net margins reached \$3.5 million. The cooperative distributed \$11.2 million in cash payments to members, \$5.2 million to marketing, warehouse and pool patrons, \$943,000 in stock retirements

and about \$5.1 million for retiring per-unit retains.

The Mission Valley Fabrics facility was converted to yarn spinning, denim weaving and finishing due to a heavy flow of cheap, imported textiles and apparel from Asia. All denim weaving was relocated to PCCA’s American Cotton Growers plant at Littlefield, Texas. “The improved denim market enabled us to work more closely with our major customer and we have expanded our customer list to insulate us from any single customer having a difficult time in the market,” May said. New denim products and finishes, he noted, increased flexibility in meeting customer needs and improving earnings.

---

## Meeting the Challenge *continued from page 6*

damaging as any failure in financial oversight.

**5. Seek efficient structures.** As farmers and cooperatives enter the 21st century, traditional structure is under severe pressure. When profit margins are thin, internal conflicts among the layers of decision makers in a federated system—as each strives to capture what margins there are—can become debilitating. Also, assets are tied up in farm supply manufacturing facilities and grain elevators that might be better deployed in information technology and value-added food processing.

Large, federated cooperatives are facing intense competitive pressure. In some cases, smaller, centralized associations will be able to function with less capital and to make management decisions relatively quickly. When these associations see an opportunity that is beyond their reach, they may be better off forming a joint venture with other cooperative and non-cooperative firms than forming a federated cooperative. This provides access to people, funding and markets not otherwise available while they continue to function as an independent cooperative organization.

Farmer-members must ask themselves some fundamental questions: Do they have to own physical assets they can see and touch? Can they operate in an environment of shared control and benefits? Can they allow their cooperative businesses to evolve and change?

**6. Forge a strong public policy presence.** Government decisions will play an important part in the future of cooperatives. Farmers and cooperatives will receive few favorable laws or administrative decisions just because they think they deserve them. Good policy outcomes, like good business outcomes, are usually the result of careful planning and hard work.

In the 21st century, cooperatives must enhance their role in protecting and advancing the political interests of farmers.

This includes educating legislators regarding how cooperatives might receive stronger support in terms of access to and assistance from federal and state programs. It also means collaborating with program administrators to make sure producer-members receive the maximum benefit, or suffer the least possible harm, from public sector initiatives.

### **7. Make decisions based on cooperative principles.**

The core cooperative principles (user-ownership, user-control and user-benefit) make the cooperative a unique form of organization with distinct characteristics, strengths and difficulties. While all three principles are important, the concept of user-control seems most critical to operating on a cooperative basis. As cooperative members struggle to adjust to the demands of the 21st century, they may find that flexibility is necessary to protect the continued availability of a cooperative presence in the industries where they do business. But only through continued user control can the members ensure that these deviations from the norm don’t transform their “cooperative” into just another investor-owned firm. It is through control that members ensure business outcomes consistent with their goals for their cooperatives.

Control is the ability to make the decisions that determine how the entity conducts itself. Member-users can have 100 percent of the voting rights and still give away control to management, lenders, outside equity holders or advisors. To increase the likelihood of success for the greatest number of cooperatives in the 21st century, the single most critical recommendation of those who participated in USDA’s focus group meetings is this: cooperatives must have highly competent directors who understand how to exercise effective control over their cooperatives and do so in a manner that promotes the best interests of the member-users. ■

## **GROWMARK turns 75 with sales of \$1.3 billion**

It started with the delivery of rail tank cars of kerosene destined for Illinois farms in the 1920s. Seventy-five years later, GROWMARK recorded earnings of \$17.5 million on sales of \$1.3 billion in the midst of a nationwide downturn in many parts of agriculture. Member companies will share patronage refunds of \$14.4 million for 2002. Those marks are down from fiscal 2001, when the cooperative showed earnings of \$18.3 million based on sales of \$1.4 billion.

While National Cooperative Refinery Association (NCRA) provided \$14.4 million in petroleum patronage, a depressed fertilizer industry prevented the co-op from collecting patronage refunds from CF Industries, a fertilizer manufacturing company it is part owner of. UPI, an Ontario-based petroleum company owned jointly by GROWMARK and Sonoco, provided a \$1 million dividend to the cooperative. Member companies will share \$1 million in patronage from the feed alliance with Land O'Lakes. Grain volume through a joint venture formed 17 years ago with Archer Daniels Midland was up 3 percent.



*GROWMARK is supplying its member co-ops with soybean-based diesel fuel and lubricants. Photo courtesy GROWMARK*

CEO Bill Davisson has set twin goals of increasing revenue while controlling costs. One goal is to earn \$15 million before patronage from NCRA and CF. "Profitable growth will come from increased market share with all members and increased number of members in an expanded geography," he said. "The GROWMARK system deals in a \$60 billion market in our core geography. A market share increase of just 1 percent across our system could result in a sales increase of \$60 million and, in turn, produce the \$15 million income goal." Increased share has accompanied geographic growth in recent years.

Davisson said meeting the income goal would help the cooperative revolve equity in accordance with its base plan "to keep ownership in the hands of those who rely on their regional cooperative. It would build the system's base capital through retained earnings, providing both a safety net in cyclical downturns and a resource base to allow us to capitalize on opportunities."

Chairman Dan Kelley credited progress to concentrating on the cooperative's core business in agronomy, energy and grain marketing. He said the cooperative needed to strengthen its seed area because "better seed technology will be an important addition over the next 5 to 10 years."

Meanwhile, the cooperative has begun supplying its member companies with soybean-based lubricants based on technology developed by researchers at the University of Northern Iowa in 1991. Environmental Lubricants Manufacturing Inc. was formed to transfer the technology into commercial soy-based products, such as bar/chain and gear lubricants, truck grease and industrial and tractor hydraulic fluids. The lubricants are biodegradable and less toxic than tra-

## **Negotiating the crossroads** *continued from page 9*

- maintain a strong balance sheet and promote member investment in the co-op;
- reduce system costs;
- don't try to be all things to all people;
- a mature industry warrants change, but position the co-op prudently;
- work to keep the cooperative system (your system) viable and strong; and
- keep up with farming trends, seeking opportunity where feasible.

One of the implicit themes in each of these lessons is cooperative education. Education about your cooperative—how it is uniquely structured and governed, how it fits in the marketplace, how it adds to a strong overall

cooperative system and how it affords benefits to members that would be sorely missed if it were gone.

This education and communication effort must consistently be provided to current members, prospective members and even to the general public in communities where your cooperative conducts business. Educational initiatives with 4-H, FFA and other youth groups are especially important. Directors are strongly reminded to do their utmost to keep well versed and educated about the increasingly complex issues faced in carrying out your critical duties and responsibilities.

Each one of you—whether a director, management team member, employee or member—must be an "educator" in the true sense of the word.

Finally, when we have seen cooperatives falter, it is important to recognize that it is because of a business problem, not a cooperative problem. The current problems with a depressed economy have hit farmers especially hard and have presented new challenges and problems to solve in cooperative businesses. Rather than pretend that these issues do not exist, or will soon go away and that things will always stay the same, board members, working in concert with management, must forthrightly direct attention to them.

I hope all of us here today understand that the cooperative model of doing business remains strong and a valid means for farmer-members to work together for their economic good. ■

ditional lubricants made from petroleum.

More than 15 millions gallons of soy biodiesel were sold by 35 member cooperatives this spring. Nearly 75 percent of the gasoline sold in the GROW-MARK system contained ethanol.

Davisson said the renewable "home-grown fuels" are good for the environment, agriculture and in reducing our dependence on foreign sources of fuel.

#### **CHS nets \$126 million**

CHS Cooperatives reported net income of \$126 million for fiscal 2002,

down more than \$50 million from 2001. But CEO John Johnson said performance was ahead of budget for every major business unit of the Minnesota cooperative. Consolidated sales of \$7.73 billion were near the \$7.75 billion mark for 2001.

"As we pursue our vision as an agricultural supply and grain-based foods system, CHS will continue to measure decisions on future projects and acquisitions against our priorities of maintaining a solid financial foundation and investment-grade balance sheet," John-

son said. CHS handled 1.2 billion bushels of grain, the eighth consecutive year the cooperative has moved more than 1 billion bushels. Earnings in agronomy, country operations, grain marketing, oil seeds processing and foods were ahead of 2001, as were earnings from processed grains and foods. Wheat milling operations were shifted into Horizon Milling LLC, a joint venture with Cargill Inc. CHS owns 24 percent of the venture. Energy earnings also were significantly ahead of budget.

---

### **What went wrong at Agway?** *continued from page 15*

restructuring plan called for exiting several profitable businesses to raise cash to reduce debt, a red flag. Another warning was Agway's failure to sell its leasing division Telmark, which led to severe financial distress for the co-op, the report said.

Agway's announcement on June 14 that it would no longer repurchase subordinated debt was yet another warning sign, as was the simultaneous resignation of Agway's two outside, non-member board directors in June. There was no press release announcing their resignation, another red flag, the report said.

Agway also filed its annual report and required SEC filing as late as pos-

sible. It hadn't done that in other years.

The report says that while Agway is struggling, the cooperative remains a major competitive force in the Northeast and helps drive down prices for all farmers.

Members, directors and managers are all accountable for Agway's troubles, the report concludes: Members have asked Agway to do too much without considering the costs involved; directors didn't always demand profitable results; and managers sometimes selected the wrong strategies.

Agriculture has changed in the past 30 years, as has the way farmers buy their supplies.

"The market has changed quickly

and dramatically for supply cooperatives, and Agway was slow to react," Anderson said. "We think they just didn't move quickly enough."

Agway's Hoefer agreed that the consolidation and concentration of agriculture has changed rapidly.

"In some cases, we've been slower than the marketplace in our response," he said. "But there have been a lot of challenges in response to those changes in agriculture." Agway officials received a copy of the report as a courtesy, the professors said. ■

*The Herald Co, Syracuse, N.Y., 2002; The Post-Standard; All Rights Reserved; Used with permission.*

---

### **Focus On ...** *continued from page 26*

keting members pay a per-acre fee for this service.

**New Tools:** Rising levels of participation in UFM resulted in the co-op turning to a local computer programmer to create a new database. This software program allows producers to review hypothetical marketing scenarios, weighing benefits against profitability objectives. It includes key customer financial information, such as financial obligations, farm history (including yield and revenue), crop insurance revenue guarantees and expected prof-

itability based on net present value. At any point, producers can see the result of forward pricing, ag options and current price vs. what the expected profitability outcome would be. This then can be weighed against expectations.

Co-op leaders credit the computer program with helping to keep participation retention in the program running in the high 90-percentile range. UFM recently entered into a contractual arrangement to sell this software to AgVantage Software, in Rochester, Minn., which is marketing it as part of a package with other

existing software for producers.

**Contact phone:** (217) 964-2111; fax: (217) 964-2260; Web site: [www.ursacoop.com](http://www.ursacoop.com); e-mail: [rlhugen@adams.net](mailto:rlhugen@adams.net). ■

The "Focus on..." section of the magazine is intended to showcase cooperatives that are finding innovative ways to deal with a marketing or member services challenge. If you would like to see your co-op featured in this space, please send an e-mail, briefly stating how you are meeting a key challenge, to: [dan.campbell@usda.gov](mailto:dan.campbell@usda.gov), or call the editor at (202) 720-6483.

# Cooperative Education for **EVERYONE!**

## ON YOUR MARK!

To show people why they might want to be part of a cooperative, give them a copy of this brochure explaining the benefits of being a co-op member: CIR-54.



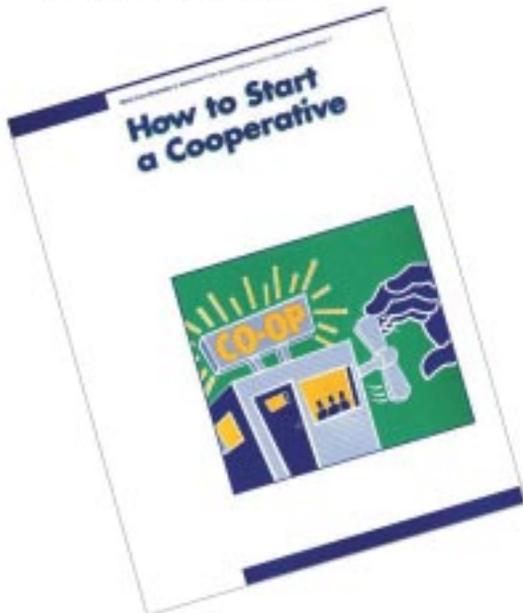
## GET SET!!

When somebody is ready to learn more about what makes a co-op special and how cooperatives work, they need *Co-ops 101*, CIR-55.



## GO!!!

When a group decides there's a co-op in their future, they'll want to do it right. For step-by-step directions, turn to *How to Start a Cooperative*, CIR-7.



Download from our website at [www.rdev.usda.gov](http://www.rdev.usda.gov).  
Or, fill out the order form below and send or fax to:

USDA/Rural Business-Cooperative Service  
1400 Independence Avenue, SW  
STOP 0705,  
Washington, D.C. 20250-0705.

Telephone: Area Code (202) 720-8381  
FAX Number: Area Code (202) 690-4083  
E-mail: [coopinfo@usda.gov](mailto:coopinfo@usda.gov)

### Yes! Send me:

- \_\_\_\_\_ copies of Co-op Information Report 54:  
**Join a Cooperative.**
- \_\_\_\_\_ copies of Co-op Information Report 55:  
**Co-ops 101**
- \_\_\_\_\_ copies of Co-op Information Report 7:  
**How to Start a Cooperative.**

Name \_\_\_\_\_  
Address \_\_\_\_\_  
City \_\_\_\_\_  
State \_\_\_\_\_ Zip \_\_\_\_\_

